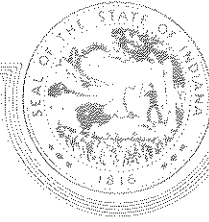


STATE OF INDIANA

DEPARTMENT OF REVENUE
OFFICE OF THE COMMISSIONER
INDIANA GOVERNMENT CENTER NORTH
100 NORTH SENATE AVENUE, ROOM N248



INDIANAPOLIS, 46204-2253

October 19, 2012

Scott Peterson
Executive Director
Streamlined Sales Tax Governing Board
4219 Hillsboro Pike, Suite 234
Nashville, TN 37215

Dear Scott:

This letter is in response to the memorandum concerning the preliminary report on 2012 annual recertification for Indiana.

The report recommends that Indiana add several citations to the Taxability Matrix. We have updated the Taxability Matrix to conform to the recommendations.

Report Comment: Ancillary services – add same citations to sub-categories.

Response: Indiana has submitted a revised Taxability Matrix, which now includes the statute citations in the sub-categories.

Report Comment: Grooming and hygiene products. The statute does not define over-the-counter drugs or grooming and hygiene products. The statute exempts drugs, which includes over-the-counter drugs, with a prescription. The taxability matrix shows grooming and hygiene products as taxable with no comment regarding those that meet the definition of over-the-counter drugs with a prescription.

Response: Under Indiana law, sales of tangible personal property are subject to sales tax unless specifically exempted by a statute. Indiana statutes do not provide an exemption from sales tax for “grooming and hygiene products.” Therefore, Indiana asserts that a definition of these items is not necessary. IC § 6-2.5-1-17 defines a “legend” drug. IC § 6-2.5-5-19 distinguishes legend drugs from “nonlegend drugs.” IC 6-2.5-5-19 also exempts from sales tax both legend and nonlegend drugs if sold under a doctor’s prescription. Therefore, Indiana has not made, nor needs to make, a distinction for over-the-counter drugs or grooming and hygiene products.

However, Indiana has added a note to its Taxability Matrix providing clarity with respect to grooming and hygiene products: “grooming and hygiene products that meet the definition of ‘over-the-counter drugs’ are exempt if sold under a prescription and the person who uses the over-the-counter drug is confined to a hospital or a health care facility.”

Report Comment: Requests change of code cites or entries in the certificate of compliance with regard to the following:

Section 303, third and fourth questions – Indiana agrees with recommendations, and changed IC 6-2.5-11-2 to IC 6-2.5-11-5;

Section 304 – Indiana agrees with recommendation, and changed IC 6-2.5-11-11 to IC 6-2.5-11-10;

Section 322, all questions after A – Indiana agrees with recommendation, and added "N/A";

Section 330, paragraph A – Indiana agrees with recommendation, and added IC 6-2.5-4-15;

Section 502, paragraph E – Indiana agrees with recommendation, and changed IC 6-2.5-11-10 to IC 6-2.5-11-12;

Under Appendix C, Library of Definitions, Vertical service – Indiana agrees with recommendation, and changed IC 6-2.5-1-27.5 to IC 6-2.5-1-11.3.

Report Comment: Federal taxes exempt from sales tax.

Response: The cited statute exempts “retailer's excise tax imposed by the United States,” and “manufacturer's excise tax imposed by the United States” on specified categories of vehicles and other tangible personal property if either collected or stated separately. The Department acknowledges and recognizes a need to examine its exclusion of certain excise taxes from the calculation of sales tax on transactions involving motor and special fuel.

Report Comment: Direct mail sourcing

Response: The applicable Indiana sourcing statute does not incorporate the recent expansion provided in the SSUTA. In its recommendations to the General Assembly, the Department of Revenue will suggest amending IC 6-2.5-13-3 to adopt the two different methods of direct mail sourcing for “advertising and promotional materials” and “other direct mail.”

Report Comment: Rounding rule.

Response: The Department cited the rounding rule for this Section; however, that statute does not include a provision that allows the seller to elect to compute the tax due based on an item or invoice basis. The statute requires the tax to be based on the gross retail income of the transaction. The Department expresses concerns that a fact pattern allowing a seller to compute the tax due on an item by item basis could result in significant tax evasion if a seller prices each individual item less than the threshold for the state to impose tax, but the sale of several items based on an invoice would result in the proper amount of tax due. For example, seller taxes on an item basis and sells 1,000,000 nails to a home builder, but sells them for \$.04 each. If sold on an

item basis there would not be any sales tax collected, but if sold on an invoice basis, there would be \$2,800 in sales tax due.

Report Comment: Accepting a SER from a Model 4 seller.

Response: In its efforts to expand SER administration to Model 4 sellers, the Department hopes to conclude the testing phase by the end of 2012. Successful completion of that phase should allow Model 4 sellers to file SERs in early 2013.

Report Comment: Blood glucose meters.

Response: The Department asserts that the language added to the notes section to clarify that the exemption for free samples of prescription drugs includes prescription drugs, drugs containing insulin or an insulin analog, and blood glucose monitoring devices provides guidance to sellers and purchasers. However, the Department will also include a suggested change to IC 6-2.5-5-18 in its recommendations to the General Assembly.


BAC Report Comment: The Indiana Department of State Revenue has issued rulings, e.g., Revenue Ruling #2009-03 ST (released 4/29/2009), taking the position that prewritten software that is licensed for use and available from a remote server is taxable. Indiana's attempt to tax access to prewritten software (and any associated hardware) from a customer merely accessing the prewritten software that is not delivered (i.e., downloaded) to the customer as a sale of "tangible personal property" is not compliant with the SSUTA. While the definition of "tangible personal property" specifically includes "prewritten software," § 333 of the SSUTA excludes computer software, which prewritten software is a component of, from the term "products transferred electronically." This is an important distinction because, as pointed out in Rule 332.2.B.4, the term "transferred electronically" is broader than the term "delivered electronically" that is used in computer related definitions. That rule specifies that just accessing a product can be considered something "transferred electronically;" however, this provision cannot apply to prewritten software because § 333 of the SSUTA excludes it from being a product "transferred electronically." It also, logically, does not fit in as tangible personal property based on the SSUTA sourcing provisions for tangible personal property. When prewritten software is only accessed by a purchaser, there is no "[t]aking possession of the tangible personal property" as specified § 311.A of the SSUTA (defining when something is "received"). Further, if it is found that Indiana can tax access to prewritten software based on it being "transferred electronically," the requirements in § 332.D of the SSUTA must be met. Absent Indiana having a law (i.e., statute), the tax on such software only reaches transactions where the purchaser: 1) has a right of permanent use, 2) has no obligation to make continued payments and 3) is an end user. Accordingly, while Indiana may choose to tax access to prewritten software by specifically imposing a tax on the sale of such product, Indiana cannot do it via the SSUTA's definition of tangible personal property and remain compliant with the SSUTA.

Response: While the Department of Revenue recognizes BAC concerns, the Department asserts that its sales and use tax treatment of remote access to prewritten computer software remains in compliance with SSUTA. The Department also recognizes and respects the Governing Board's instruction to SLAC to form a workgroup specifically to address remote access to prewritten

computer software. That instruction necessarily came in response to both BAC and the States seeking clarification of, and simplification to, the arguments raised by BAC. That workgroup's preliminary conclusion to the Governing Board at the September 2012 meetings in Salt Lake City stated that "[t]he SSUTA allows States to tax remote access to pre-written computer software by taxing it as a sale or use of tangible personal property."

If you have any further questions, please do not hesitate to contact Larry Molnar at (317) 233-0656.

Sincerely,

A handwritten signature in black ink, appearing to read "Mike Alley". The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

Mike Alley
Commissioner