BEFORE THE GEORGIA TAX TRIBUNAL
STATE OF GEORGIA

FEB 11 2015

Yvonne Bouras
Tax Tribunal Administrator

INGLETT & STUBBS INTERNATIONAL, LTD.,	)	
Petitioner,	)	
v.	)	**TAX TRIBUNAL DOCKET NO. TAX – IIT - 1340253**
LYNETTE T. RILEY, COMMISSIONER OF THE GEORGIA DEPARTMENT OF REVENUE,	)	
Respondent.	)	

DECISION

2015 – 2 Ga. Tax Tribunal, February 11 , 2015

This case is a refund suit filed by Inglett & Stubbs International, Ltd. ("Petitioner") pursuant to O.C.G.A. §§ 48-2-35 and -35.1 seeking a refund of state and local sales and use taxes it paid to vendors from February 1, 2010 through November 30, 2011, on its purchase of electrical materials, vehicles, safety equipment, and office supplies used in the construction of electrical facilities at the Bagram and Kandahar bases in Afghanistan pursuant to its contract with the federal government.

Petitioner initially sought its refund on the grounds that the items at issue were purchased for resale to the federal government. The Department of Revenue ("Department") denied this refund claim. In its appeal to this Tribunal challenging that denial, Petitioner has raised an additional argument as a basis for its refund claim – that most of these items were, in fact, purchased outside the state of Georgia and use tax is not due because the items only had a "momentary presence" at Petitioner's Georgia facility.

Resolving this case requires us to revisit several fundamental issues under the Georgia Sales and Use Tax Act. The first is the key concept of "sale for resale" and the question of whether contractors like Petitioner can ever purchase tangible personal property "for resale." Unfortunately for Petitioner, as will be discussed below, under the laws of Georgia, a contractor, such as Petitioner, is *per se* deemed to be the consumer of the items of tangible personal property it purchases in the performance of its contracts. Accordingly, Petitioner's purchases of property that were made in Georgia cannot be purchases for resale and are therefore taxable.

The second issue is whether the storage of property acquired by Petitioner in transactions made in interstate commerce results in a taxable use of that property when it is stored in Georgia prior to being shipped to Afghanistan. In the final analysis, this issue likewise turns on the rule that a contractor is deemed *per se* to be the user of tangible personal property which it purchases, that such property cannot be held for resale, and, as a consequence, such storage and repackaging of such tangible personal property in Georgia is a taxable use.[1]

Accordingly, Petitioner's Motion for Summary Judgment must be **DENIED** and Respondent's Motion for Summary Judgment must be **GRANTED**.

I. FINDINGS OF FACT

The facts in this matter are contained in a Joint Stipulation of the parties, several affidavits and depositions. They are not disputed.

[1] Due to the basis on which this case is being decided, certain other issues raised by the parties, including various procedural issues as to elements of Petitioner's refund claim, are not addressed in this decision.

A. Petitioner's Business and its Contracts for International Projects

Petitioner is an international service provider and contractor based in Smyrna, Georgia. Petitioner was formed for the purpose of performing overseas military contracts. It provides electrical construction and services in international locations.

In December 2004, Petitioner was awarded a U.S. Department of the Army ("Army") contract for the construction and installation of electrical distribution systems at military airfields in Bagram and Kandahar, Afghanistan. A second, substantially similar, contract was awarded in December 2010. Both of these contracts are referred to collectively as the "Contract."

The Contract is a master contract known as an IDIQ (indefinite delivery, indefinite quantity). The IDIQ format allows the Army to determine over time which projects it would like to have performed pursuant to the Contract and put those projects out for proposal to selected contractor(s).

When the Army desires to have a project done pursuant to the Contract, it issues a request for proposal for the work. Petitioner responds to the request for proposal by

(a) compiling a "bill of materials" necessary to complete the project based on Petitioner's experienced forecast of necessary purchases;

(b) using the compilation to compute a lump sum price for the project; and

(c) submitting its bid to perform the project for the lump sum price to the Army.

The Army then decides whether to accept Petitioner's bid. If it does, the Army issues a "task order" reflecting the work to be accomplished and the agreed upon total price for the completion of the work. Petitioner would then invoice the Army based upon the agreed upon price for the work: typically 30 to 40 percent of the price when the materials first reached Afghanistan, and then the remainder over time.

Under the Contract, Petitioner was required to compile its bid using certain parameters. Under one of these parameters, Petitioner marked up the cost of projected materials to be acquired by a 7% premium. This mark-up was only applied to the materials that would actually become part of the completed installation – not the equipment, tools, and office supplies. Since this bid was a projection, Petitioner would often discover that it needed to purchase different materials at different prices than those originally projected. If it did so, it would simply absorb any of the difference in price.

After receiving a task order, Petitioner purchases the property needed for the project from third-party vendors. Petitioner does not purchase property related to work performed under the Contract if it is not associated with a particular task requested by the Army. All of the items at issue in this case were ordered based on a task requested to be performed by the Army. In addition to the Contract, Petitioner had three other contracts during the audit period for the performance of electrical construction work in Iraq.

For income tax purposes, all items of tangible personal property that Petitioner acquired for purposes of fulfillment of the contract were accounted for on Petitioner's books as a "cost of goods sold" for accounting purposes.

Petitioner does not contract with any party to furnish tangible personal property or to perform services within the United States. Petitioner does not fabricate, repair, modify, assemble or alter the property at issue in this case in the United States, including the state of Georgia. Petitioner does not use the property purchased pursuant to the Contract to construct, alter, repair or modify real property in the state of Georgia.

B. Shipment of the Property to Afghanistan

Petitioner times its placement of orders with its vendors based upon when the item ordered will be needed for a project at the overseas Army bases. Some items that Petitioner purchases are shipped directly by its vendors to the overseas Army bases, and other items are either shipped or delivered to Petitioner's distribution facility in Smyrna, Georgia. In general, larger items, such as turbines, are shipped directly to Afghanistan, while smaller items are shipped or delivered to the Smyrna facility.

All of the items at issue in this case arrived at Petitioner's Smyrna facility, FOB destination (these items will be referred to as the "Property"). Petitioner maintains documentation for every purchased item that is received in its Smyrna facility in the ordinary course of business. The information captured includes the date the item is received at the Smyrna facility and the task name with which the purchase is associated.

All Property that is received at the Smyrna facility is shipped to the overseas Army bases, as all Property is shipped or delivered to the Smyrna facility for the sole purpose of being shipped to one of the international project sites. None of the Property remains in Georgia or elsewhere in the United States. Shipping the Property is expensive – it costs as much to ship the Property overseas as it does to purchase the Property itself.

When the Property arrives at the Smyrna facility, it is kept in its original packaging. The Property is picked up from the Smyrna facility by a common carrier trucking company and is taken directly to the airport for ultimate shipment to the U.S. Army bases in Afghanistan. Petitioner maintains documentation of all shipments of the Property to the overseas Army bases in the ordinary course of business. Shipping documentation includes the shipping invoice, job reference sheet, packing list and pickup receipt. Each shipment receives a tracking number, and

Petitioner records the date that each shipment of the Property is received in Afghanistan in the ordinary course of business.

While at the Smyrna facility, the Property may be moved to a different pallet, other than the one it arrives upon, for shipment to Afghanistan in order to (a) obtain the right weight and dimensions of a pallet to maximize shipping efficiencies for overseas delivery, and (b) occasionally to group materials for a particular task together on a pallet.

During the period at issue, shipments to Afghanistan were generally scheduled for each Monday and Thursday. In order to maximize efficiency of the overseas shipments, some Property may be held in the Smyrna warehouse for days or weeks prior to being shipped to Afghanistan. The average time period between when the Property arrived at the Smyrna facility and when it was received at the overseas Army bases was 21 days. The average amount of time the Property was in transit between Georgia and the overseas Army bases was four days. Once the Property is delivered to the overseas base, Petitioner invoices the Army for an agreed upon percentage of the price on the task order, usually 30 or 40 percent. Petitioner records the cost of the Property on its books and records as "costs of goods sold" for tax and accounting purposes.

Under the Contract, Petitioner was also responsible for storing the materials during the performance of each project and taking unused materials from the site once the work is completed. Petitioner would sometimes ship unused materials and equipment from one federal project to another.

C. Procedural History

On February 17, 2012, Petitioner requested a refund of sales/use tax that had been paid to its vendors for the periods February 1, 2010 through November 30, 2011 (the "Audit Period") in the amount of $2,010,820, plus interest as may be allowed by law. After reaching certain

agreements between the parties and certain adjustments, the parties stipulated that the current amount included within the refund request was $1,955,794.97. A further adjustment was agreed to by the parties prior to oral argument, further reducing the aggregate amount in dispute by $43,890.93 to $1,911,904.04.

All of the invoices at issue in this case reflect Georgia sales tax charged to Petitioner. The parties have divided the invoices within the requested refund into certain categories by vendor, including:

(a) invoices for purchases that occurred within the state of Georgia,

(b) invoices for purchases where the invoice provides that the item was delivered to Petitioner's Smyrna facility in the vendor's truck,

(c) invoices for purchases that were shipped from outside the state to Petitioner's Smyrna facility, and

(d) invoices for purchases where the items were shipped to Petitioner's Smyrna facility via common carrier, for which the origination point of the shipment is disputed between the parties.

Petitioner's refund request was accompanied by waivers from some of its Georgia-registered vendors certifying that the vendors did not and would not claim refunds of the same tax included in Petitioner's refund request. At the time of the filing of the refund claim, Petitioner's refund request did not include waivers from the following vendors:

(a) Flint Electric Company,

(b) HD Supply,

(c) HD Supply Electrical,

(d) HD Supply Plumbing/HVAC,

(e) Power Plan,

(f) Rexel, and

(g) Staples Advantage.

Petitioner subsequently provided waivers from HD Supply, HD Supply Electrical, HD Supply Plumbing/HVAC and Staples Advantage to the Department at an in-person meeting while the refund claim was pending. After the refund claim was denied, but prior to briefing and argument in this case, Petitioner supplied an additional waiver from Rexel to the Department.

Respondent denied Petitioner's request by letter dated December 6, 2012. The stated basis for the Department's denial of Petitioner's refund claim was that Petitioner is a contractor governed by O.C.G.A. § 48-8-63(b).

After the refund claim was denied, Petitioner filed a Petition in the Georgia Tax Tribunal, on May 15, 2013. In its Petition, Petitioner raised a new argument that a portion of the Property was purchased out of state, and that use tax on that Property was not owed because the items were only "momentarily" in Georgia.

Pursuant to the Case Management Order in this matter, the parties filed cross motions for summary judgment and supporting briefs on June 13, 2014, and subsequent reply briefs. This case was argued on August 27, 2014. As noted above, at oral argument, the parties agreed to some slight additional adjustments further reducing the principal amount at issue.

II. CONCLUSIONS OF LAW

A. Jurisdiction and Venue

The Tribunal has jurisdiction over this appeal from the Department's denial of Petitioner's claim for refund pursuant to O.C.G.A. §§ 48-2-35(c)(4) and 50-13A-9(a). Venue is proper before the Tribunal pursuant to O.C.G.A. § 48-2-35(c)(4).

B. Standard of Review on Summary Judgment

The standards governing summary judgment are well established. To prevail at summary judgment under O.C.G.A. § 9-11-56, the moving party must demonstrate that there is no genuine issue of material fact as to each element of its claim and that the undisputed facts, viewed in the light most favorable to the nonmoving party, warrant judgment as a matter of law. O.C.G.A. § 9 11-56(c); Lau's Corp., Inc. v. Haskins, 261 Ga. 491 (1991); H. Alan Rosenberg, 2014 - 15 Ga. Tax Tribunal, November 25, 2014.

Proceedings before the Tribunal are *de novo* in nature, and the evidence on the issues in a hearing before the Tribunal is not limited to the evidence presented to or considered by the Department prior to the Department's decision. O.C.G.A. § 50-13A-14; see Ga. Comp. R. & Regs. 616-1-3-.11 as adopted in Standing Order dated June 1, 2013.

C. Law and Analysis

As noted earlier, ultimately the decision in this case turns upon the question of whether a contractor can ever be treated as purchasing tangible personal property which the contractor purchases in order to fulfill a contract as purchasing such items for resale. As will be seen, Georgia law provides that a contractor is conclusively deemed to be the consumer of such items and cannot qualify such purchases as non-taxable purchases for resale.

1. The complementary nature of Georgia sales and use taxes.

The Georgia General Assembly enacted the Georgia Retailers' and Consumers' Sales and Use Tax Act in 1951 (the "Act"). Ga. Laws 1951, p. 360 (enacted by Act 240). When enacted, these sales and use taxes replaced nearly 400 license and excise taxes of various kinds on business activity. When the Act was signed into law on February 20, 1951, then Governor

Herman Talmadge also signed House Bill 2 repealing all of the existing license and excise taxes. The original act was located at Chapter 92-34A of the "Unofficial Code" because when the Act was passed, there was no "official" Code of Georgia. The sales and use tax statutes ("Georgia Sales and Use Tax") were eventually re-codified and incorporated into the Official Code of Georgia Annotated as Title 48, Chapter 8 of the Georgia Code by Act 795, Laws 1978.

One of the broad conceptual principles underlying the Georgia Sales and Use Tax is to impose sales (or the complementary use) tax on the ultimate consumer of tangible personal property or the enumerated services that are specified to be taxable under the statute. O.C.G.A. § 48-8-30.[2]

The tax is thus imposed upon the sale to the ultimate end-user of the taxable personal property or taxable services. Under well-settled constitutional jurisprudence, the states cannot impose sales tax on sales occurring in interstate commerce. McCleod v. J.D. Dilworth Co., 322 U.S. 327 (1944). So in order to tax purchases that arise from sales occurring in interstate commerce, Georgia imposes a complementary use tax on the first incidence of use within the state of property purchased in interstate commerce. Thus the applicable provisions of the Georgia Public Revenue Code impose sales and use tax upon the retail purchase, retail sale, rental, storage, use, or consumption of tangible personal property. See O.C.G.A. §§ 48-8-2(8), (9), (12) & (13); 48-8-30(a)-(c).

A critical issue for determining when a sale of tangible personal property is taxable as a "retail sale" is the definition of retail sale. Under O.C.G.A. § 48-8-2(31) "retail sale" or "sale at

[2] Although the term "end user," which is a term that is used in common parlance today, was not generally used at the time of the enactment of the original sales and use tax, use of that term is helpful in understanding the underlying theoretical structure of the sales and use tax. Conceptually, the statute, with various exceptions that arise on the particular facts, is designed to impose the sales or use tax as appropriate on the ultimate purchaser or consumer of

retail "means any sale, lease, or rental for any purpose *other than for resale*, sublease, or subrent." (emphasis added). The definition of taxable "retail sale" is thus a negative definition. A retail sale is any sale of tangible personal property "other than for resale."[3]

2. Taxation of transactions involving sales of both tangible personal property and services.

One of the recurrent questions under the Georgia Sales and Use Tax Act is how sales and use tax applies to transactions involving the sale of tangible personal property in connection with the delivery of services.

Perhaps the seminal case addressing this issue is Craig-Tourial Leather Co. v. Reynolds, 87 Ga. App. 360 (1952). In Craig-Tourial, the action actually arose as a dispute between a wholesaler and a retailer. Id. at 363. The wholesaler sold leather products and shoe findings to the defendant shoe repair company. Id. at 361. The question for determination was whether the sale by the plaintiff to the defendant of goods that were to be used in repairing and mending shoes was a sale at retail, such as would require the plaintiff to collect from the defendant the Georgia sales and use tax, or purchases for resale to the customer. Id. at 363.

The court concluded that the repair company was indeed the consumer of the products in question. Id. at 368. As a consequence, the court reasoned that the sale from the wholesaler to the shoe repair company was in fact a taxable retail sale rather than a sale for resale. Id. The court noted that "[s]hoe repairs may reasonably be said to fall within the category of 'personal service transactions' and it may be inferred from the stipulation of fact that the defendant shoe

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the items of tangible personal property or services. Such ultimate consumer can often be thought of handily as an "end user" in common parlance.

[3] It is often erroneously said that a sale for resale is "exempt" under Georgia sales and use tax. Similarly, references to the "resale exemption" are common in the literature (indeed on applicable forms such as the Department's Form ST-5 Sales Tax Certificate of Exemption). But it is technically incorrect to refer to a "resale exemption," however.

repairman does not make separate charges for materials used and for the services rendered in making shoe repairs." Id. at 364-65.

Although the court duly noted that the value of the materials used in making the repairs constituted a significant component of the total charge to the ultimate purchaser of the repairs, the court adopted a "for the purpose of the customer" test to determine whether the transaction should be viewed as a sale of a service or of a purchase of tangible property.

> However, we think the main consideration should be the purpose of the customer, who primarily wishes to buy the skilled services of shoe repairman because such services cannot be performed by the customer himself because he lacks the equipment, time, or skill required. Under such circumstances, the sale of various grades or qualities of materials by the shoe repairman is really incidental to and but a means of rendering the services which his customers want.

Id. at 365.

Interestingly and of great importance for the future administration of the Georgia sales and use tax, however, the court also went on to note, that if the charges for the materials had been separately stated, the result might have been different.

> If a shoe repairman, such as the defendant, should desire to conduct his business by separating the price of the materials he uses from the price of the labor to apply the materials to his customers' shoes, so as to resell or retail, in effect, shoe findings to his customers apart from his services, it appears that he would be free to do so. If he were to register as a seller and certify that he is purchasing for resale, then he would not be required to pay the tax to the plaintiff distributor, but would be required to collect the tax himself, as a dealer or retailer, from his customers, on the price of the shoe findings sold to them. Ga. L. 1951, pp. 370, 386 (Code, Ann. Supp., §§ 92-3408a, 92-3444a). But if, as in the present case, the shoe repairman conducts his business as it is ordinarily conducted, without making separate charges for labor and for materials, then he must pay the tax on the materials bought to the person from whom he purchases them, i.e., the plaintiff.

Id.

Strictly speaking, a sale for resale is not exempt from sales and use tax--it is simply excluded from the definition of taxable sales.

There are numerous situations where the issue is how to tax such "mixed" transactions which combine sales of potentially taxable tangible personal property with sales of otherwise non-taxable services is addressed by statute or regulation. Thus, for instance, O.C.G.A. § 48-8-3(22) exempts from sales and use tax sales of professional, insurance or personal service transactions which involve sales as inconsequential elements for which no separate charge is made. Hawes v. Dimension, Inc. 122 Ga. App 190, 191-93 (1970) (Architectural models are not taxable). In such circumstances, the party providing such services is the consumer and such purchases are taxed when the service provider purchases such items. Similarly, there are a number of instances where, by regulation, taxpayers are permitted to identify and limit tax to tangible personal property that is sold in various transactions which involve the sale of tangible personal property in connection with provision of services. By separately stating and charging tax on the tangible personal property they are able to avoid taxation on the associated services.[4]

3. Taxation of contractors under the Georgia sales and use tax.

Against this background, the key question in this case is whether a contractor such as Petitioner is the *per se* purchaser of the tangible personal property that it purchases in connection with the performance of its contract or whether, alternatively, a contractor such as Petitioner can avail itself of the rule that permits service providers to treat tangible personal property that they

[4] Examples are numerous. These include repairs, alterations and repair parts, (see Ga. Comp. R. & Regs. 560-12-2-.78(2013)), freight, delivery and transportation charges in certain circumstances (see Ga. Comp. R. & Regs. 560-12-2-.45 (2013)), labor in installing, applying, remodeling or repairing tangible personal property when separately stated (see Ga. Comp. R. & Regs. 560-12-2-.88 (2013)), in certain limited circumstances freight, delivery and transportation charges (see Ga. Comp. R. & Regs. 560-12-2-.45 (2013)), and computer software and certain computer-related services (see Ga. Comp. R. & Regs. 560-12-2-.111 (2013)). Similarly, there are a number of specific industries where the regulations articulate the requirement that labor be separately stated in order to avoid the cost of such labor being included in the taxable purchase price of associated tangible personal property. See, e.g., Ga. Comp. R. & Regs. 560-12-2-.94, Cabinet Makers; Ga. Comp. R. & Regs. 560-12-2-.98,Warning, Sound and Music Devices; Ga. Comp. R. & Regs. 560-12-2-.99, Sheet Metal Contractors; and Ga. Comp. R. & Regs. 560-12-2-.66, Monuments and Memorial Stones.

have purchased as being purchased for resale to their end user customers if the charge for such property is separately stated. If Petitioner can show that the items of tangible personal property that it purchased pursuant to the Contract were purchased for resale to the Army, then the purchases are not taxable because such purchases are non-taxable purchases of tangible personal property for resale. If, on the other hand, Petitioner is viewed as the user or consumer of these items, Petitioner, not the Army as an instrumentality of the federal government, is the ultimate purchaser and the purchases are taxable as retail sales when purchased by Petitioner.

How to tax purchases of tangible personal property by contractors has been a bone of contention under the Georgia Sales and Use Tax Act since its inception. Only three years after Georgia adopted the original version of the Georgia Sales and Use Tax Act in 1951, the Court of Appeals addressed this issue in J.W. Meadors & Co. v. State, 89 Ga. App. 583, 584 (1954).

In Meadors, the taxpayer contracted to construct and improve waterworks for the City of Macon. Id. at 583. The contractor paid the sales tax on its purchases initially, and then sued for refund of that tax, contending that it purchased the items it used in the construction project for resale. Id. In rejecting the refund claim, the Court held that,

> [U]nder these facts the contractor cannot reasonably be said to have made a resale to the City of Macon of the tangible personal property as such. The contractor was compensated for a completed installation, and we surmise that the contract only separated the values of the personal property used from the other items of expense involved, because of the contention of the city that no sales taxes could be charged for the items since the city would ultimately acquire the property. A contractor when fabricating personalty into realty neither sells, resells, sells at retail, nor can he be considered a retailer. A contractor who buys building material is not one who buys and sells -- a trader. He is not a "dealer," or one who habitually and constantly, as a business, deals in and sells any given commodity. He does not sell lime and cement and nails and lumber[.] Sales to contractors are sales to consumers[.] There are authorities to the contrary, but we think that the above express the correct reasoning and conclusion.

Id. at 584 (internal citations and quotations omitted).

In Meadors, Georgia adopted the rule that contractors are consumers of the items that they purchase for use in performing their contracts. Under this view, a contractor is the *per se* end-user consumer of the tangible personal property that it purchases to perform its contracts and the purchase by the contractor is a taxable retail sale upon which tax is due at that time. Note in particular that the charges in Meadors were separately stated. Yet the court still concluded the contractor was the consumer and, therefore, the tax applied. Meadors continues to be cited as good law and Meadors is critical for the resolution of this case because Meadors antedates O.C.G.A. § 48-8-63(b).

In 1955, the year following the Meadors decision, the Georgia General Assembly enacted the predecessor to the current O.C.G.A. § 48-8-63. See 1955 Ga. Laws. 389. The portion of the amendments that is now codified as subsection O.C.G.A. § 48-8-63(b)[5] effectively codified the Meadors decision. But other provisions expanded and elaborated upon the rule that a contractor is a consumer of tangible personal properties for purposes of the sale tax statute. For instance, in addition to codifying the Meadors rule in O.C.G.A. § 48-8-63(b), to ensure that the contractor-as-consumer rule of Meadors could not be "end-run" by consumers engaging the contractor to provide services when the owner supplied the items to be used in performing the contract, the amendments added O.C.G.A. § 48-8-63(c). This section provides:

> Each person who contracts to perform services in this state and who is furnished tangible personal property for use under the contract by the person, or such person's agent or representative, for whom the contract is to be performed, when a sales or use tax has not been paid to this state by the person supplying the tangible

[5] "Each person who orally, in writing, or by purchase order contracts to furnish tangible personal property and to perform services under the contract within this state shall be deemed to be the consumer of the tangible personal property and shall pay the sales tax imposed by this article at the time of the purchase. Any person so contracting who fails to pay the sales tax at the time of the purchase or at the time the sale is consummated outside the limits of this state shall be liable for the payment of the sales or use tax. This Code section shall not relieve the dealer who made the sale from such dealer's liability to collect and pay the tax on purchases by a contractor." O.C.G.A. § 48-8-63(b).

> personal property, shall be deemed to be the consumer of the tangible personal property so used and shall pay a use tax based on the fair market value of the tangible personal property so used irrespective of whether any right, title, or interest in the tangible personal property becomes vested in the contractors.

The effect of O.C.G.A. § 48-8-63(c) is to reiterate that a contractor that falls under the statute is *always* the consumer and the user of the property, even if the ultimate owner of the property for whom the work is being done purchases the materials and supplies these to the contractor, unless the party supplying the materials has already paid the tax.

In 1968, the Georgia courts were called upon to determine whether the "contractor is a *per se* consumer" rule of Meadors applied to contractors who contract to build structures outside the State of Georgia. In the case of Macon Mach. Shop, Inc. v. Hawes, 118 Ga. App. 280 (1968), the taxpayer had entered into a contract as a subcontractor for Blount Brothers Construction Company for the construction of certain steel structures on property of the Federal Atomic Energy Commission in Oak Ridge, Tennessee. Id. at 280. The materials used in this contract were withdrawn from inventory maintained in Macon, Georgia, fabricated as necessary, and shipped to Tennessee for installation. Id. at 280-82. On appeal, the Department of Revenue made the same argument that it makes here –that items purchased in Georgia by a contractor are purchased at retail regardless of whether the construction occurs in this or another state. Id. The Court of Appeals held the taxpayer liable stating:

> Where raw materials are fabricated by a contractor into products to be installed and incorporated into realty, this constitutes a "use" or "consumption" by the contractor, who is liable for the tax regardless of the fact that the entity with whom it is contracting is a political subdivision exempt from the payment of sales tax. "Sales to contractors are sales to consumers." J.W. Meadors & Co. v. State of Ga., 89 Ga. App. 583, 585 (80 SE2d 86). Is the situation different because, after the materials were fabricated in Georgia, the taxpayer installed them on real property located in another state?

Id. at 281-82. The Court answered no, reaffirming the rule established in Meadors that items purchased by a contractor for use in performing a contract are considered purchased at retail – not for resale – due to the nature of the contractor's business, a rule that applies regardless of where the construction actually occurs. Id. at 282-84; Strickland v. W.E. Ross & Sons, Inc., 251 Ga. 324, 325 (1983) ("Contractors must pay the sales tax on this tangible personal property at the time they purchase it."); see also Hawes v. Nat'l Serv. Indus., 121 Ga. App. 775, 778 (1970) (noting that the ruling in Macon Machine Shop provides that "withdrawal of raw materials from inventory in Georgia and their fabrication by the contractor into structural entities which it subsequently installed in Tennessee" is a taxable event).

While the cases subsequent to Meadors can be distinguished factually from the unusual facts presented here, under Meadors, which continues to be good law, contractors are conclusively deemed consumers and end-users of items that they purchase within this state. As such contractors such as Petitioner owe sales tax on those in state purchases regardless of where the installations subsequently occur.[6]

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[6] It should be noted that the contractor as *per se* consumer rule can have results that appear to be at odds with policies underlying other provisions of the Revenue Code. For instance, in Meadors, the case arose out of a situation where the construction services were being provided to a municipality. Normally, purchases by municipalities for its own use would not have been taxable.

Likewise, in Resourcing Serv. Atlanta LLC v. Georgia Dep't of Revenue, 288 Ga. App. 532 (2007), the taxpayer argued that because it made its purchases as an agent for a hospital authority which was an entity exempt from sales tax, the taxpayer was not itself subject to the imposition of the sales and use tax on the items it purchased on behalf of the authority because it was not a "contractor" within the meaning of O.C.G.A. § 48-8-63(b). Id. at 532. The court, however, accepted the Respondent's position that the purchaser was a contractor within the meaning of this statute and the tax was therefore due. Id. at 534. The court noted, interestingly, that the effect of its decision was to impose a tax which would not have been due had the Authority purchased the items directly. Id.

> Although RSA contends it is not seeking a 'derivative' exemption based upon its relationship with the Authority, taken together its arguments show that such a result is what it seeks. Such an exemption, however, does not exist under Georgia law. Even though RSA accurately argues that, because it is acting as an agent of the Authority, its purchases are essentially the Authority's purchases, we have found no provision in our law in which the General Assembly has created such an exemption. Therefore, the superior court correctly concluded that the Department's imposition of sales and use taxes upon RSA was correct under Georgia law. Any contention that, because of

Petitioner argues forcefully that this conclusion cannot be correct when applied to Petitioner because Petitioner does not provide services under the Contract within this state as required by O.C.G.A. § 48-8-63(b). Petitioner correctly points out that the Contract and transactions performed under it are not within the purview of O.C.G.A. § 48-8-63(b) because Petitioner's only contracts are international and are performed overseas. O.C.G.A. § 48-8-63(b) provides, in relevant part:

> Each person who orally, in writing, or by purchase order contracts to furnish tangible personal property and to perform services under the contract *within this state* shall be deemed to be the consumer of the tangible personal property and shall pay the sales tax imposed by this article at the time of the purchase. Any person so contracting who fails to pay the sales tax at the time of the purchase or at the time the sale is consummated outside the limits of this state shall be liable for the payment of the sales or use tax.

O.C.G.A. § 48-8-63(b) (emphasis added).

The corresponding regulation similarly provides as follows:

> Any person who contracts to furnish tangible personal property and perform services thereunder in constructing, altering, repairing or improving real property *in this State* is deemed to be the consumer of all tangible personal property used or consumed in performing such contract and shall pay the tax thereon at the time of purchase, use, storage or consumption in this State, whichever occurs first.

Ga. Comp. R. & Regs. 560-12-2-.26(1) (emphasis added).

Petitioner correctly points out that by their terms, neither O.C.G.A. § 48-8-63(b) nor the regulation is applicable to Petitioner, an international contractor and servicer whose only contracts are for work outside the United States.[7] However, as noted above, the rule of Meadors

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> public policy considerations, Georgia should have a derivative exemption from O.C.G.A. § 48-8-63 for hospital authorities must be resolved by the General Assembly and not this court.

Id. at 534-35.

[7] To reach the conclusion that O.C.G.A. § 48-8-63(b) applies to Petitioner, the statute would need to have be written as follows: "Each person *within this state* who orally, in writing, or by purchase order contracts to furnish

that a contractor is always deemed to be a consumer predates the provisions of O.C.G.A. § 48-8-63(b). There is no indication that the 1955 amendments that added the codified section were intended to overrule or limit Meadors. To the contrary, the legislation builds upon and expands the rule adopted by the court in Meadors and the amendments are consistent with it. And as noted above, the Meadors case has been cited favorably numerous times since that time.

Accordingly, the conclusion that Petitioner's purchases of tangible personal property within the state of Georgia that are to be installed pursuant to contracts to be performed exclusively in Afghanistan are taxable because Petitioner is a contractor is unavoidable.

4. The applicability of Georgia use tax to items purchased in interstate commerce and stored at Petitioner's warehouse prior to shipment to Afghanistan.

Petitioner alternatively contends that a large portion of its refund claim, $1,285,829.62[8] of the $1,911,904.04 stipulated to be remaining in dispute, is related to purchases made outside the state of Georgia, and that Georgia use tax was not due because the items had only a "momentary presence" in the state before being shipped to Afghanistan. Thus, Petitioner contends that a large portion of the tax it remitted to its vendors was, in fact, use tax remitted on sales made in interstate commerce, and that it is entitled to a refund of this portion of the tax.

Georgia sales tax is due when tangible personal property is sold at retail within this state "regardless of any subsequent employment or use thereof in interstate commerce." Ga. Comp. R. & Regs. 560-12-2-.54; O.C.G.A. § 48-8-30(b). By contrast, use tax is due upon the first instance of use, consumption, distribution, or storage within the state of items purchased at retail outside the state. See O.C.G.A. § 48-8-30(c).

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tangible personal property and to perform services under the contract shall be deemed to be the consumer of the tangible personal property and shall pay the sales tax imposed by this article at the time of the purchase."

It is undisputed that every item of Property in this case, including items purchased from non-Georgia vendors, was shipped or delivered to Petitioner's Georgia warehouse, F.O.B. destination. Those purchases that were made in interstate commerce are not subject to Georgia sales tax under well-settled constitutional jurisprudence. Quill Corp. v. North Dakota, 504 U.S. 298 (1992); American Oil Co. v. Neill, 380 U.S. 451 (1965); Gen. Trading Co. v. State Tax Comm'n of Iowa, 322 U.S. 335 (1944); McCleod v. J.D. Dilworth Co., 322 U.S. 327 (1944). Such items, if taxable in Georgia, are taxable under the Georgia use tax. See Hawes v. Nat'l Serv. Indus., Inc., 121 Ga. App. 775.

Under O.C.G.A. § 48-8-30(c), use tax is due upon the first instance of use, consumption, distribution, or storage within the state of items purchased at retail outside the state. "Use" is defined as "the exercise of any right or power over tangible personal property incident to the ownership of the property . . . ." O.C.G.A. § 48-8-2(40). "Storage" means any "keeping or retention in this state of tangible personal property for use or consumption in this state *or for any purpose other than sale at retail in the regular course of business.*" O.C.G.A. § 48-8-2(35) (emphasis added). The use tax is thus owed if Petitioner exercised any right or power over these items of Property purchased from out-of-state vendors within this state, including keeping or retaining them, irrespective of whether those items were subsequently shipped out of state.

It is undisputed that Petitioner used and stored these items in its Smyrna warehouse. Indeed, the parties have stipulated that the items at issue could be held in Petitioner's warehouse for days or weeks. And significantly, many of the items once received at the warehouse were reorganized and combined for shipping. This is important because a key function of performance

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[8] $252,340.69 of this amount relates to vendors for which Respondent contends Petitioner did not comply with the provisions of the refund statute.

by Petitioner under the Contract was minimizing shipping costs because the shipping costs were so large relative to the value of the items of personal property. Thus, Petitioner made a taxable use of such Property and the Georgia use tax applies.

Stated a bit differently, *if* Petitioner were not a contractor and as such were not deemed *per se* to be the consumer of these items of the Property, then Petitioner would have been able to qualify the purchases of the Property in interstate commerce as purchases for resale to the Army. As such, Petitioner would hold the Property in its warehouse for "*sale at retail in the regular course of business*" under O.C.G.A. § 48-8-2(35). If Petitioner were not the *per se* consumer, Petitioner would not have made a taxable use of such property in Georgia by storing and repackaging it for resale and such purchases would not be taxable. But, as a *per se* consumer under Meadors, Petitioner cannot qualify as reselling such items of Property to the Army. Such purchases are therefore taxable under the use tax when Petitioner stores, retains and reorganizes them for shipment in Petitioner's warehouse in Smyrna.

It should be noted that this conclusion is consistent with the underlying structure of the Sales and Use Tax Act. The use tax is complementary of the sales tax. Transactions that would be taxable under the sales tax but are not taxable because they occur in interstate commerce are taxable under the use tax if they would have been taxable in Georgia had the transactions occurred in Georgia. Ga. Comp. R. & Regs. 560-12-2-.54(1)(b). Given the conclusion that sales tax is due on purchases of Property from Georgia vendors to be used in fulfilling the Contract, it is appropriate that the same result applies to items purchased by Petitioner from non-Georgia vendors that are stored and reorganized in Petitioner's warehouse prior to being shipped to Afghanistan for installation.

Accordingly, because under Meadors Petitioner is the *per se* consumer of the Property that was purchased in interstate commerce, Petitioner used that Property when it stored and reorganized it in its warehouse in Smyrna. Use tax was therefore due and Petitioner is not entitled to refund of the use tax imposed on those items.

5. Because certain language in the Department of Revenue's Regulation is inconsistent with the statutory language, the Regulation is not controlling on this issue.

The resolution of the issue with respect to the applicability of Georgia use tax to Petitioner's purchases from out of state vendors turns upon the conclusion that the contractor as *per se* consumer rule applies to Petitioner, which, when read with O.C.G.A § 48-8-2(40), establishes that such items are taxable. As a consequence, certain language in Ga. Comp. R. & Regs. 560-12-2-.54(1)(b), which provides that the use tax does not apply unless "such property has become a part of the mass of the property in this State" is not controlling. This is fortunate for Respondent because the Department's regulation on this point is at odds with the current statute and, if controlling, would result in Petitioner prevailing on this issue.

Georgia law regarding the application of use tax to items purchased outside the state of Georgia has changed significantly over the years. From February 9, 1951 until February 9, 1965, the Georgia statutes provided that,

> It is not the intention of this Act to levy a tax upon articles of tangible personal property imported into this State or produced or manufactured in this State for export, the repairing or storage of such property in the State for use in another State, nor is it the intention of this Act to levy a tax on bona fide interstate commerce.
> It is, however, the intention of this Act to levy a tax on the sale at retail, the use, the consumption, the distribution, and the storage to be used or consumed in this State of tangible personal property after it has come to rest in this State and has become a part of the mass of property in this State.

1951 Ga. Laws 360, § 4; 1965 Ga. Laws 13, § 2.

Thus, before 1965, the fact that the property was brought into this state for export was sufficient to exempt it from tax. In 1965, however, the General Assembly amended the statute to broaden it significantly, substituting the following language for the above-quoted language in its entirety:

> It is the intention of the General Assembly in enacting this Act to exercise its full and complete power to tax the retail purchase, the retail sale, the rental, the storage, the use and the consumption of tangible personal property and the services herein described, except to the extent prohibited by the Constitutions of the United States and of Georgia and to the extent of specific exemptions provided elsewhere in this Act.

1965 Ga. Laws 13, § 2. Since then, this statute has again been amended and provides, as noted above, that tax is due "upon the first instance of use, consumption, distribution, or storage within this state of tangible personal property purchased at retail outside this state" irrespective of whether the property is subsequently shipped outside of the state. O.C.G.A. § 48-8-30(b).

This amendment is significant because a number of the early cases interpreting the application of the use tax to items shipped from outside the state do so under the prior law. See Hawes v. Nat'l Serv. Indus., Inc., 121 Ga. App. 775, 777 (1970) ("The Commissioner relies on the original language of the Sales and Use Tax Act in respect to transactions before the approval of the amendment on February 19, 1965."); Undercofler v. E. Airlines, Inc., 221 Ga. 824, 829 (1966) (noting that whether tax should be imposed "hinges upon the proper construction of a provision of Section 4 of the Georgia Retailers' and Consumers' Sales and Use Tax Act (Ga. L. 1951, p. 360, as amended; Code Ann. Ch. 92-34A), as it existed prior to February 19, 1965"). Among these cases is Macon Mach. Shop v. Hawes, 118 Ga. App. 280, 282 (1968), in which the Court distinguishes Undercofler on the grounds that the items at issue in Macon Machine Shop were withdrawn from inventory in Georgia and fabricated here before being shipped to

Tennessee. Compare Hawes, 121 Ga. App. at 777-78 (pursuant to the "in and out" exclusion of section 4 of the pre-1965 Act, mere storage of property brought into the state to be used in another state is not taxable).

This history of legislative change makes it all the more curious that Respondent's regulation Ga. Comp. R. & Regs. 560-12-2-.54(1)(b) continues to contain language stating that the use tax applies to "[t]he first use in Georgia of tangible personal property bought elsewhere in a transaction which would have been taxed had the transaction occurred in Georgia, *provided such property has become a part of the mass of the property in this State* . . . ." Id. (emphasis added). And even more surprisingly, the regulation was re-promulgated in 1990, long after the statutory changes to which Respondent now points. The language regarding "mass of property within the state" provides for a significantly more limited scope to the Georgia use tax than Respondent is urging here. Not surprisingly, Respondent has disavowed at least this part of her Department's regulation in this case. Petitioner argues persuasively that under this language in the regulation, were it controlling, Petitioner should prevail.

It is unusual, and indeed a bit ironic, for Respondent to disavow her own agency's regulation while the Petitioner urges its application. The shoe is generally on the other foot with Respondent arguing the court should give deference to the administrative agency in the interpretation of regulations implementing a statute due to the Department's presumed expertise.[9]

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[9] When Respondent wants a regulation to apply to a situation, Respondent's argument usually runs along the lines of the following: The State Revenue Commissioner has explicit authority to promulgate regulations "for the enforcement of [the Public Revenue Code] and the collection of revenues [thereunder]." O.C.G.A. § 48-2-12(a). See generally Georgia Oilmen's Association v. Department of Revenue, 261 Ga. App. 393, 395 (2003) ("all of the rules challenged . . . in these appeals are authorized generally by O.C.G.A. § 3-2-2(a) of the Alcoholic Beverage Code . . . , which permits promulgation of 'reasonable rules and regulations not inconsistent with this title or other laws.'") Georgia Oilmen's Association v. Georgia Dep't of Revenue, 261 Ga. App. 393, 398-99 (2003). Indeed, "if [a] statute is silent or ambiguous with respect to a specific issue, the question for the court is whether the agency's [regulation] is based on a permissible construction of the statute," Georgia Dep't of Revenue v. Georgia Chemistry Council, 270 Ga. App. at 617 n.7 (quoting Chevron U.S.A. v. Natural Resources Defense Council, 467 U.S. 837,

This case is thus illustrative of the dangers of unthinking reliance on the language of a regulation or undue deference to asserted administrative expertise. Here, the regulation as written appears to be based upon the prior statute, not the current version of the law. A regulation cannot change the statute. Dep't of Human Res. v. Anderson, 218 Ga. App. 528 (1995) ("an administrative rule which exceeds the scope of or is inconsistent with authority of the statute upon which it is predicated is invalid.") When a tax statute is unambiguous, regardless of whether it imposes a tax or provides an exemption or credit, its plain meaning must be enforced as written with no strict construction against either party. See, e.g., Chatham Cnty. Bd. of Tax Assessors v. Bock, 299 Ga. App. 257, 259 (2009) ("If the language is plain and does not lead to any absurd or impractical consequences, the court simply construes it according to its terms and conducts no further inquiry."); Lowry v. McDuffie, 269 Ga. 202, 204 (1998) ("[I]f the language of a statute is plain and susceptible of but one natural and reasonable construction, the court has no authority to place a different construction upon it, but must construe it according to its terms."); Richmond Cnty. Bd. of Tax Assessors v. Ga. R.R. Bank & Trust Co., 242 Ga. 23, 24 (1978) (same). As noted above, the statutory language coupled with consistent application of the Meadors rule leads to the conclusion that the use tax is due on items of Property purchased in interstate commerce and stored at Petitioner's facility even though the Department's regulation indicates otherwise.

III. CONCLUSION

For the reasons discussed above, the Commissioner's Motion for Summary Judgment is **GRANTED** in its entirety and Petitioner's Motion for Summary Judgment is **DENIED**.

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843 (footnotes omitted)), and "[not whether the court] would have implemented the statute in a different manner" absent a regulation on point. Miller v. United States, 65 F.3d 687, 689 (8th Cir. 1995). Fortunately for Respondent in this case, the statute is not ambiguous or else Respondent would be hoisted by her own regulatory petard on this issue.

This 17th day of February, 2015.

CHARLES R. BEAUDROT, JR.
JUDGE, *PRO TEMPORE*
GEORGIA TAX TRIBUNAL

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