

REDACTED DECISION – DK# 07-397 RC & 07-398 RC – BY – CHRISTOPHER B. AMOS, ADMINISTRATIVE LAW JUDGE – SUBMITTED FOR DECISION on JULY 28, 2009 – ISSUED ON MAY 25, 2011

SYNOPSIS

CONSUMERS SALES AND SERVICE TAX – BURDEN OF PROOF – In matters before the West Virginia Office of Tax Appeals on a petition for refund the burden of proof is upon the petitioner-taxpayer to show that there is an entitlement to the refund claimed. *See* W. Va. Code Ann. § 11-10A-10(e) (West 2010) and W. Va. Code R. §§ 121-1-62.8 and 63.1 (2003).

CONSUMERS SALES AND SERVICE TAX – SERVICES PURCHASED FOR RESALE – West Virginia imposes a general consumers sales and service tax. W. Va. Code Ann. § 11-15-1 *et seq.* (West 2010).

CONSUMERS SALES AND SERVICE TAX – SERVICES PURCHASED FOR RESALE – Vendors are required to collect consumers sales and service taxes “[f]or the privilege of selling tangible personal property or custom software and for the privilege of furnishing certain selected services defined in sections two and eight of this article[.]” W. Va. Code Ann. § 11-15-3(a) (West 2010).

CONSUMERS SALES AND SERVICE TAX – SERVICES PURCHASED FOR RESALE – “To prevent evasion, it is presumed that all sales and services are subject to the tax until the contrary is clearly established.” W. Va. Code Ann. § 11-15-6(b) (West 2010).

CONSUMERS SALES AND SERVICE TAX – SERVICES PURCHASED FOR RESALE – “‘Service’ or ‘selected service’ includes all non-professional activities engaged in for other persons for a consideration, which involve the rendering of a service as distinguished from the sale of tangible personal property . . . but does not include . . . any service rendered for resale[.]” W. Va. Code Ann. § 11-15-2(b)(18) (West 2010).

CONSUMERS SALES AND SERVICE TAX – SERVICES PURCHASED FOR RESALE – “A service is purchased for resale when it is subcontracted by the person who is contracted to perform the service” W. Va. Code R. § 110-15-33.4.5 (2003).

PROCEDURAL HISTORY

On or about January 18, 2007, and March 30, 2007, Corporation A, filed with the State Tax Department two claims for refund of consumers sales and service tax totaling \$____, for the period of January 1, 2003, through February 28, 2004. By letter dated May 10, 2007, the Sales

Tax Unit of the Internal Auditing Division of the West Virginia State Tax Department (hereinafter the Respondent), denied both claims for refund. Subsequently, on or about April 3, 2007, Corporation B., filed three claims for refund of consumers sales and service tax totaling \$____, for the period of March 1, 2004, through November 10, 2006. By letter dated May 24, 2007, Respondent also denied those claims for refund.

On July 9, 2007, Corporation A and Corporation B (hereinafter collectively the Petitioners) filed timely protests with the West Virginia Office of Tax Appeals, challenging Respondent's denial of all five claims for refund. As relief Petitioners seek \$____, the aggregate amount of sales and service tax that they assert was paid and to which they are entitled a refund. An evidentiary hearing on the merits was held at the Office of Tax Appeals in Charleston, West Virginia, on December 3, 2008, before the honorable Robert W. Kiefer, Jr., Administrative Law Judge. Petitioners were represented by legal counsel. Respondent was represented by a Staff Attorney with the West Virginia State Tax Department. For administrative reasons this matter was reassigned to the undersigned Administrative Law Judge by order dated December 1, 2010.¹

FINDINGS OF FACT

1. Petitioner, Corporation A, is a corporation duly licensed to conduct business in the state of West Virginia.

2. Petitioner, Corporation B, is a corporation duly licensed to conduct business in the state of West Virginia.

3. Petitioners are a subsidiary of Corporation C, a multinational corporation headquartered outside the United States.

4. Petitioners are engaged in the business of furnishing engineering design services through their site team located at Corporation X's facility in West Virginia.

¹ It is unclear from the record why a decision in this case was not issued earlier.

5. Petitioners and Corporation X entered into a joint venture agreement which governs the contractual arrangement between the Petitioners and Corporation X.

6. The services furnished by the Petitioners are provided pursuant to and in accordance with the requirements of the agreement with Corporation X.

7. To meet its requirements under the agreement, Petitioners maintain at Corporation X site a core group of employees, and occasionally supplements that workforce with leased employees pursuant to arrangements with various employee leasing companies (i.e., temporary employment agencies).

8. When the volume of the Petitioners' work increases they hire leased employees to handle the extra work. Likewise, when Petitioners' work volume decreases they release those temporary employees.

9. The leased employees typically have an engineering background, an engineering design background, or certain computer skills.

10. There are (9) nine temporary agencies from which the Petitioners lease employees.

11. The leased workers are employees of the leasing companies and are not employed by the Petitioners.

12. Petitioners do not directly pay the leased employees any wages, withhold federal or state taxes on them, or exercise any disciplinary authority over them.

13. The leased workers augment Petitioners' staff and perform the same type of work as the employees of the Petitioners located at Corporation X's facility.

14. The number of Petitioners' employees and the number of leased employees working at Corporation X's facility during the years 2003 through 2006 ranged from 50 to 70 at

any given time, and the number of leased employees constituted 10 to 20 percent of that number. Together, Petitioners' regular and leased employees make up their site team located in West Virginia.

15. When Petitioners refer to somebody on the site team it could be either one of Petitioner's employee's or a contract leased employee.

16. The site team manager for the Petitioners is Mr. A.

17. Mr. A decides whom to hire from the leasing companies and how many leased employees to hire.

18. Having oversight of the entire team and the work that Petitioner provides, Mr. A supervises the leased employees.

19. Mr. A is the administrative manager for the entire site team, which includes employees leased by the Petitioners.

20. Petitioners' work at Corporation X's facility begins with an idea from one of the corporations engineers. Petitioners then develop a complete design deliverable package that is handed off to a contractor who will do the work.

21. Petitioners' site team manager (Mr. A) assigns the various regular and leased employees to Corporation X's business units. The regular and leased employees complete the design work, which ultimately must be approved by a Corporation X engineer who is assigned to the project.

22. The employee leasing companies invoice Petitioners for the services of the leased employees, and to this amount the leasing companies typically add sales tax. The invoices from the leasing company are not submitted to Corporation X for payment.

23. Most of the invoices entered into the record reflect sales tax charged by the leasing companies, while it appears that at least one invoice does not.

24. Petitioners receive an invoice for the leased employees directly from the leasing company and pay the invoice directly to the leasing company, including any specifically added sales tax.

25. Petitioners remit payment to the employment agencies who in turn compensate the leased workers.

26. Petitioners invoice Corporation X on an hourly basis for the work of each individual based upon the number of hours worked by the individual during the subject time period.

27. Petitioners invoice Corporation X for the services that are furnished by both their employees and the leased employees. Petitioners do not invoice Corporation X separately for Petitioner's employees, as opposed to the leased employees.

28. Petitioners mark-up the cost of the leased employees when they invoice Corporation X

ISSUES

The issues presented here are (1) whether Petitioners resold the services of the leased employees that they utilized and would thus be entitled to a refund of consumers sales and service taxes, and (2) if the answer to that question is in the affirmative, whether Respondent raised a viable defense by arguing that there is no evidence that the leasing companies actually remitted to the West Virginia Tax Department the sales tax that they charged Petitioners.

BURDEN OF PROOF

In matters before the West Virginia Office of Tax Appeals, on a petition for refund, the burden of proof is upon the petitioner-taxpayer to show that there is an entitlement to the refund claimed. *See* W. Va. Code Ann. § 11-10A-10(e) (West 2010) and W. Va. Code R. §§ 121-1-62.8 and 63.1 (2003). Accordingly, Petitioners must establish that they are entitled to a refund of consumers sales and service taxes paid on the leased employees that they utilized to consummate their contract with Corporation X.

DISCUSSION

West Virginia imposes a general consumers sales and service tax. *See* W. Va. Code Ann. § 11-15-1 *et seq.* (West 2010). Vendors are required to collect such taxes “[f]or the privilege of selling tangible personal property or custom software and for the privilege of furnishing certain selected services defined in sections two and eight of this article[.]” W. Va. Code Ann. § 11-15-3(a) (West 2010). “To prevent evasion, it is presumed that all sales and services are subject to the tax until the contrary is clearly established.” W. Va. Code Ann. § 11-15-6(b) (West 2010). Additionally, “‘Service’ or ‘selected service’ includes all non-professional activities engaged in for other persons for a consideration, which involve the rendering of a service as distinguished from the sale of tangible personal property . . . but does not include . . . any service rendered for resale[.]” *See* W. Va. Code Ann. § 11-15-2(b)(18) (West 2010).

The portion of the tax regulations pertinent here reads in relevant part:

33.4. Enumerated Services Excepted. - Consumers sales and service tax shall not apply to any of the following services:

* * *

33.4.5. A service which is purchased for resale. A service is purchased for resale when it is subcontracted by the person who is contracted to perform the service, for example:

Example 1. X is a printer and enters into a contract with Y to print 500 bulletins. X subcontracts the job to Z. Z prints the 500 bulletins for X. There is no tax on the contract between X and Z since X is purchasing the printing service from Z for resale to Y. In this transaction Y provides the paper upon which the bulletins are printed.

Example 2. B owns a used car lot. E purchases an automobile from B. As a condition of such sale B agrees to make repairs to the automobile. However, B subcontracts such repair work to C. E has agreed to pay B for the repair services and for the sale price of the automobile. Under these circumstances, the repair services furnished by C to B constitute a sale of such service to B for resale to E who is the consumer of the services.

Example 3. B owns an auto repair shop and C brings an automobile in to have the air conditioning fixed. B is unable to fix the unit so the car is sent to G who is an air conditioning specialist. The sale of G's service to B is a sale for resale by B to C.

W. Va. Code. R. § 110-15-33.4.5 (2003).

In order to prevail on their claims Petitioners must establish that the services they purchased from various temporary employment were indeed resold to Corporation X.² In support of their position Petitioners argue that they are purchasing certain services from employee leasing companies and resell the benefits of the services to Corporation X. Petitioners assert that this arrangement is analogous to Example 3 in Section 33.4.5 of the regulations, because they are

² Respondent contends that the Petitioners are not entitled to a refund for these claims in part because they do not meet the test for any statutory exemption as set forth in West Virginia Code Section 11-15-9 *et seq.* However, the law governing claims to exemptions does not apply here because services purchased for resale are not part of the tax base in that they are specifically excluded from taxation to begin with. When the West Virginia Legislature declared that “‘Service’ or ‘selected service’ . . . does not include . . . any service rendered for resale” they evidenced an obvious intent to exclude from taxation those services that are purchased for resale. W. Va. Code Ann. § 11-15-2(b)(18) (West 2010). Therefore, Petitioners do not have to demonstrate an entitlement to, and there need be no analysis of, an exemption under West Virginia Code Section 11-15-9, *et seq.*

purchasing the services of the leased employees for resale and, as such, the purchases of those services are excepted from taxation.³

A noticeable commonality in all three examples set forth in the regulations above is that the principal vendor could not or was not willing to perform the work requested, and the job was subcontracted to another who then performed that work. Subcontract is defined as “A contract made by a party to another contract for carrying out the other contract, or a part of it.” Black’s Law Dictionary 264 (7th Ed. 2000). Corporation X contracted with the Petitioners for engineering design services, based upon the needs of Corporation X. Petitioners did not then subcontract, in whole or in part, any portion of the design services to the leased employees or the employment agencies. Unlike Example 3 of the regulations, Petitioners did not send any of the work involved in its contract with Corporation X to a third party. Nor did the Petitioners resell the benefits of the services of the leased employees to Corporation X. The Petitioners instead obtained leased employees, effectively augmenting their workforce, so that they could fulfill their obligations to Corporation X. Petitioners chose this method as a business model, and there is no actual subcontracting present in this arrangement.

The Petitioners also rely upon the case of *B B Enterprises v. Palmer*, 214 W. Va. 571, 591 S.E.2d 129 (2003), and argue that their situation is analogous to the taxpayer in that matter. In *B B Enterprises* the taxpayers were owners and operators of exotic show bars that employed dancers on an independent contract basis. Patrons of these establishments could purchase a special drink or a private dance from the show bar which would entitle them to special attention or a private performance from one of the dancers. When those purchases were made the

³ Petitioners also contend that the services of the temporary employees were rendered in West Virginia and that all of the sales taxes at issue here were collected in the state of West Virginia. See Brief of Petitioners, Pages 10 - 14. However, Respondent’s counsel subsequently stipulated to this fact, and as such all taxes in the invoices that appear in Petitioner’s Exhibit 1 is deemed to be West Virginia sales taxes. See Respondent’s Reply Brief in Support of State’s Position, Page 19.

establishment charged the patrons the requisite tax of 6% on each sale. The show bar then tendered a portion of the money from the transaction to the dancer who provided the services to the patron.

The Tax Department in that case argued that the transaction between the show bar and the dancer was taxable. The Supreme Court of Appeals agreed with the taxpayers and held that the services of the dancers were purchased by the show bar for resale to the patrons as the ultimate consumers of the services. In its opinion the Court observed:

The Taxpayers subcontract the dancing services to female dancers, who provide floor show performances for the general population of patrons who pay a cover charge as well as “special drink” and “private dance” services for those patrons who choose to pay for such services.

Id. at 576, 134.

The Court agreed that the dancing services were subcontracted and concluded that the services were resold to patrons and thus excepted from taxation. In order to reach a similar conclusion to that of *B B Enterprises*, there must first be a finding that the services were indeed subcontracted. The regulations specifically state that “A service is purchased for resale when it is subcontracted by the person who is contracted to perform the service” W. Va. Code R. § 110-15-33.4.5 (2003). Thus, as a threshold matter, the regulations require that a service purchased for resale must have been subcontracted to another individual; something, as pointed out above, that is not present in this matter. Consequently, the Petitioners’ reliance on *B B Enterprises* is misplaced.

Finally, Petitioners argue that the temporary employees were purchased for the benefit of Corporation X. Petitioners aver that, but for the needs of Corporation X, they would not have leased the additional employees that they did. However, Petitioners obtained these leased employees in order to satisfy their obligations under the agreement. Corporation X would have

benefited just the same whether the Petitioners had obtained temporary employees or instead chose to hire new employees of their own. Moreover, the Petitioners failed to offer any authority for the proposition that the utilization of temporary employees to fulfill a contractual obligation to a third party constitutes the purchase of a service for resale.

The Petitioners did not meet their burden of proof and accordingly did not establish that they are entitled to a refund of consumers sales and service taxes paid on the leased employees that they utilized to consummate their contract with Corporation X.⁴

CONCLUSIONS OF LAW

Based upon the above it is **DETERMINED** that:

1. In matters before the West Virginia Office of Tax Appeals on a petition for refund the burden of proof is upon the petitioner-taxpayer to show that there is an entitlement to the refund claimed. *See* W. Va. Code Ann. § 11-10A-10(e) (West 2010) and W. Va. Code R. §§ 121-1-62.8 and 63.1 (2003).

2. West Virginia imposes a general consumers sales and service tax. *See* W. Va. Code Ann. § 11-15-1 *et seq.* (West 2010).

3. Vendors are required to collect consumers sales and service taxes “[f]or the privilege of selling tangible personal property or custom software and for the privilege of furnishing certain selected services defined in sections two and eight of this article[.]” W. Va. Code Ann. § 11-15-3(a) (West 2010).

4. “To prevent evasion, it is presumed that all sales and services are subject to the tax until the contrary is clearly established.” W. Va. Code Ann. § 11-15-6(b) (West 2010).

⁴ Because Petitioners did not establish that they are entitled to a refund of consumers sales and service tax in this matter, the secondary issue outlined *supra* need not be addressed.

5. “‘Service’ or ‘selected service’ includes all non-professional activities engaged in for other persons for a consideration, which involve the rendering of a service as distinguished from the sale of tangible personal property . . . but does not include . . . any service rendered for resale[.]” W. Va. Code Ann. § 11-15-2(b)(18) (West 2010).

6. “A service is purchased for resale when it is subcontracted by the person who is contracted to perform the service” W. Va. Code R. § 110-15-33.4.5 (2003).

7. To prevail in this matter the Petitioners must establish that they indeed subcontracted all or a portion of the design services to other individuals who performed that work.

8. Petitioners did not establish that they are entitled to a refund of consumers sales and service taxes paid on the leased employees that they utilized to consummate their contract with Corporation X.

DISPOSITION

WHEREFORE, it is the final decision of the West Virginia Office of Tax Appeals that the Petitioners’ claims for refund, dated on or about January 18, 2007; March 30, 2007; and April 3, 2007; in the aggregate amount of \$_____ are **DENIED**.