1991

Union Pacific Railroad Company v. Auditing Division, Utah State Tax Commission : Reply Brief

Utah Supreme Court

Rick Carlton; assistant attorney general; attorney for appellee.
Robert A. Peterson; Van Cott, Bagley, Cornwall & McCarthy; attorney for appellant.

IN THE SUPREME COURT OF THE STATE OF UTAH

UNION PACIFIC RAILROAD COMPANY, Petitioner-Appellant, vs. AUDITING DIVISION, UTAH STATE TAX COMMISSION, Respondent-Appellee.	Case No. 910150

REPLY BRIEF OF APPELLANT

On Appeal From The Order Of
The Utah State Tax Commission

Rick Carlton
Assistant Attorney General
36 South State Street, 11th Floor
Salt Lake City, Utah 84111

Attorney for Appellee

Robert A. Peterson
VAN COTT, BAGLEY, CORNWALL
& McCARTHY
50 South Main Street, #1600
Salt Lake City, Utah 84145

Attorney for Appellant

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Robert A. Peterson
VAN COTT, BAGLEY, CORNWALL & McCARTHY
50 South Main Street, #1600
Salt Lake City, Utah 84145

Attorney for Appellant

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ARGUMENT

A. THE PURCHASE OF BALLAST AND DIESEL FUEL FROM A UTAH VENDOR DOES NOT GIVE RISE TO SALES TAX IN THE CIRCUMSTANCES OF THIS CASE

Respondent argues that Union Pacific purchases of ballast and diesel fuel from Utah vendors is a "taxable event" and thus is subject to a sales tax.

The argument of Respondent is that because the sellers were not "concerned" with whether the materials were shipped outside the state and because the seller did not contract with the Union Pacific as common carrier to deliver the materials out of state, the requirements of Utah Admin. Code R. 865-18-44S(90) has not been met.

The argument advanced by Respondent totally ignores the plain language of part C of Rule 44(S) which states:

> Where delivery is made by the seller to a common carrier for transportation to the buyer outside the state of Utah, the common carrier is deemed to be the agent of the vendor for purposes of this section regardless of who was responsible for the payment of the freight charges.

The crucial provisions of the Rule are that the delivery is made by seller to a common carrier for transportation to the buyer outside the state, regardless of who pays the freight charges. The Rule does not require that the seller contract with the common carrier, only that it deliver to the common carrier.

Appellee's argument proves too much. In situations in which sales are clearly exempt, there would be a "taxable event" and, thus, sales taxes payable if Appellee's argument were accepted. Typically, the out-of-state purchaser purchases the goods from Utah sellers and remits the price of sale to the Utah seller. That, within the reasoning of the statute, constitutes a "taxable event." However, if the seller tenders the goods to a common carrier for delivery outside the state of Utah, no sales tax is payable regardless of the fact that a "taxable event" has occurred. That is true whether the sale price includes amounts paid for delivery by common carrier or whether those charges are paid separately by either the seller or the purchaser.

Searching for the occurrence of some "taxable event" does not help with the necessary analysis. In fact, the import of subsection C of Rule 44S clearly is that if a "taxable event" analysis be appropriate, the taxable event would be delivery <u>by the common carrier</u> to the out-of-state purchaser because the common carrier is by statute deemed to be the agent of the vendor, <u>regardless</u> of whether the vendor or purchaser contract with it.

The facts established that the delivery by the seller was to the Union Pacific <u>as common carrier</u>. The waybill summaries (Exhibit 2) so indicated. The testimony of the witnesses was also unrefuted that the Union Pacific accepts this material <u>as a common carrier</u>. (Transcript, p. 18, 35.)

Respondent cites the case of Tummurru Trades v. Utah State Tax Comm'n, 802 P.2d 715 (Utah 1990) in support of its argument. That case, however, did not involve the crucial subsection C of Rule 44S. In the Tummurru case, there was no delivery to a common carrier by a seller for transportation out-of-state. Further, the Tummurru case involved a situation in which the purchaser purchased materials, held them in inventory and subsequently used them. The Union Pacific did not purchase the ballast for inventory and did not place it into inventory. Rather, the ballast was delivered by the seller directly to the common carrier.

Respondent further argues that the Union Pacific cannot avoid its tax liability by a chameleon like change from common carrier to purchaser. There is nothing either mysterious or suspicious about Union Pacific's acting both as a common carrier and as a purchaser. In this case, the Union Pacific in order to have the same rights as any other similar purchaser--i.e. one who purchases material for delivery out-of-state of the same size and quantity--must be able to act in both capacities or it would be deprived the same rights as all other tax payers.

Were the Union Pacific to deliver the ballast to the Denver & Rio Grande Railroad or the Southern Pacific Railroad in Nevada or Oregon, those entities would not be subject to the sales tax. There is no reason why the Union Pacific Railroad should be disadvantaged simply because it is the only common

carrier capable of delivering the products in an economical fashion.

B. THE TAX COMMISSION ASSESSING SALES TAX ON THE MILLING SERVICES RENDERED OUT-OF-STATE IS NOT ALLOWABLE UNDER EITHER UTAH OR FEDERAL LAW

The Union Pacific in this case does not contest that it must pay sales tax on railroad ties purchased outside the state of Utah which are then shipped for use inside the state of Utah. In fact, Union Pacific did pay such a sales tax. However, the auditing division added to that purchase price an increment specifically attributable to milling charges paid by the Union Pacific for services rendered outside the state of Utah (Transcript at p. 48).

In response, the Respondent stated on page 19 of its brief that "there was no testimony nor other documentation before the Tax Commission which indicated that the milling services were performed or billed separately from the creosote treatment process of the ties. Further, the state took the position that "the treatment involved installing tangible personal property in connection with other tangible personal property."

Neither of these statements is true. The costs for milling were clearly segregated. Moreover, the milling costs were not "installation costs" but rather costs paid for services rendered outside the state of Utah. These charges had nothing to

do with "repairing or renovating personal property" as claimed by Appellee. (Brief of Appellee at p. 12 and 13)

For Utah to purport to affix a sales tax to services rendered by a vendor in the state of Oregon would be in excess of the constitutional limits imposed on Utah's power to levy sales taxes. The foundational case on this issue is Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977). In Complete Auto, the United States Supreme Court set forth a four part test for analyzing commerce clause challenges. In order to sustain a tax, it must be shown that "(1) the tax is applied to activities with a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to the services provided by the state." Id. at 7279. The tax in question fails the first and second parts of the Complete Auto analysis.

The activity which the Tax Commission is attempting to tax are services which were completely performed in Oregon. The taxable sale of the railroad ties occurred prior to the time that the milling services were rendered. Those services were *independent from the purchase and, although Oregon can clearly* tax those activities, the services have no nexus whatsoever with the state of Utah. Therefore, the tax fails the first part of the Complete Auto test.

Because the tax fails the first part of Complete Auto, it necessarily fails the second part of the test. Because the

services are performed within Oregon, Oregon can tax those services. Utah, however, has no right to tax those services and cannot fairly apportion its tax to include those services. Moreover, Utah's attempt to tax those services creates the probability that the activities will be taxed twice. (Whether or not Oregon actually taxes those services is not determinative). Armco Inc. v. Hardesty, 467 U.S. 638, 644 (1984).

Under Complete Auto, Utah may not tax those activities in question because they are completely performed from outside of the state and have no nexus with the state of Utah. Utah simply cannot tax services rendered in all states on personal property just because that personal property subsequently may be found in the state of Utah. If so, Utah could tax repair of furniture subsequently shipped to Utah, tax services performed on cars and trucks that later come to Utah, tax repairs on office equipment that later comes to Utah, etc.

The statute in question clearly contemplates by its language that the vendors performing such services will reside in the state of Utah. In this case, they do not.

For all of the above reasons, Petitioner respectfully submits that the service charges in question are not subject to Utah sales tax.

C. THE TAXES IMPOSED SHOULD NOT INCLUDE ANY PENALTY

Under Utah law, it is within the discretion of the Tax Commission to assess penalties for the failure to pay taxes if

the taxpayer was at least negligent. See Robert H. Hinckley v. Utah State Tax Comm'n, 404 P.2d 662, 669 (Utah 1965). In this case, the Tax Commission made no finding whatsoever that Petitioner was negligent or otherwise culpable with respect to the dispute involved as a payment of taxes herein. The Audit Division simply added penalties to the taxes that the Tax Commission had found payable.

Because the Tax Commission made no finding of negligence nor did it conclude that penalty should be paid, it is improper that they be added by independent act of the Audit Division subsequent to the Rule and ordered by the Tax Commission

CONCLUSION

For the foregoing reasons, Petitioner respectfully requests that it be given the following relief:

1. The imposition of sales and use taxes by the Tax Commission with respect to the purchase of ballast and fuel for use outside of the state of Utah should be reversed;

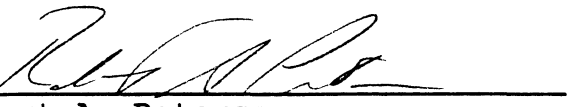
2. The imposition of a sales or use tax with respect to milling services performed outside of the state of Utah should be reversed;

3. The Tax Commission should be ordered to deduct from the costs of repair of railroad cars any costs attributable to materials on which a Utah sales tax has already been paid; and

4. The case should be remanded to the Utah Tax Commission with an Order that taxes previously paid by the Union Pacific, including penalty and interest, be refunded.

DATED this 16th day of October, 1991.

VAN COTT, BAGLEY, CORNWALL & McCARTHY

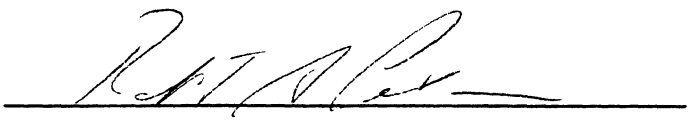
By 

Robert A. Peterson
Attorneys for Petitioner-Appellant
50 South Main Street, Suite 1600
P. O. Box 45340
Salt Lake City, Utah 84145
Telephone: (801) 532-3333

CERTIFICATE OF SERVICE

I hereby certify that I caused four true and correct copies of the within and foregoing REPLY BRIEF OF APPELLANT to be hand delivered this 16th day of October, 1991, to the following:

Rick Carlton
Assistant Attorney General
36 South State Street, Suite 1100
Salt Lake City, Utah 84111



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