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Olson Construction Co. et al v. State Tax Commission of Utah : Brief of Petitioners

Utah Supreme Court

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In the
Supreme Court of the State of Utah

FILED

V 29 1960

OLSON CONSTRUCTION COMPANY,
THIOKOL CHEMICAL CORPORATION,
Utah Division; EMPIRE
STEEL COMPANY and FIFE
ROCK PRODUCTS COMPANY,

Petitioners,

— vs. —

THE STATE TAX COMMISSION
OF UTAH,

Respondent.

Supreme Court, Utah

Case
No. 9362

BRIEF OF PETITIONERS

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OF UTAH,

Respondent.

Case
No. 9362

BRIEF OF PETITIONERS

STATEMENT OF THE CASE

For convenience, the parties herein will be designated as follows: Petitioner, Olson Construction Company as "Olson"; Petitioner, Thiokol Chemical Corporation, Utah Division, as "Thiokol"; Petitioner, Empire Steel Company as "Empire"; Petitioner, Fife Rock Products Company as "Fife"; and Respondent, State Tax Commission of Utah as the "Tax Commission." Emphasis, where used, has been supplied.

This is a proceeding to review a Decision of the Tax Commission denying a claim for refund of Sales Tax filed³ by Petitioners. The question presented is whether sales of personal property to a contractor who is constructing facilities for the Federal Government are exempt from sales and use tax in the State of Utah where the contracts involved provide for the vesting of title to all materials in the Federal Government upon delivery to the job site. In other words, are such sales for resale and therefore exempt from taxation under Chapter 15 of Title 59, Utah Code Annotated, 1953, and the regulations promulgated by the Tax Commission thereunder?

STATEMENT OF FACTS

In General:

The facts are not in dispute. A Stipulation of Facts was entered into by the parties and made a part of the record in the proceedings before the Tax Commission (R. 6). From this stipulation, the following facts appear:

Thiokol Chemical Corporation, Utah Division (hereinafter referred to as "Thiokol") holds a prime contract with the United States Government for the construction of a certain project known as the Minuteman Facilities near Brigham City, Utah. In connection with the construction of this project, Thiokol advertised and solicited bids for the construction of certain buildings and other items of said facilities. Two subcontracts were awarded to Olson Construction Company, one of said contracts being dated December 13, 1958, and the other being dated December 24, 1958. The prime contract between

Thiokol and the United States is included in the record as Exhibit "A" and the full contents of the subcontracts with Olson are set forth in Exhibits "B" through "E" inclusive.

In connection with the performance of its contracts with Thiokol, Olson purchased materials from various vendors between December, 1958, and January, 1960. In connection with these material purchases, Olson was compelled to pay to its various vendors Utah sales tax on the materials and supplies purchased for said projects. Petitioners have alleged that the total amount of sales tax which Olson paid in connection with the two contracts above described was the sum of Seventeen Thousand Eight Hundred Fifty Six Dollars and Eighty-eight Cents (\$17,856.88). Of said amount, it is stipulated that the sum of Five Thousand Fifty Three Dollars and Twenty-five Cents (\$5,053.25) was paid to Empire Steel Company and Three Thousand Seven Hundred Five Dollars and Fifty-six Cents (\$3,705.56) was paid to Fife Rock Products Company. Because of the regulations of the Commission requiring that the party who paid the tax to the State of Utah make the claim for refund, Empire Steel Company and Fife Rock Products Company were made parties to the Petition and only the recovery of the sales tax paid to the said vendors is in dispute at this time.

Pursuant to the terms of its contracts with Olson, Thiokol has reimbursed Olson for the amount of sales tax paid by Olson in connection with the performance of said contracts, including the amounts paid as sales tax to Empire Steel Company and Fife Rock Products Com-

pany. Thiokol is therefore also a party to this matter and will be directly affected by the final decision in this case.

It was stipulated that during the performance of the contracts Olson did not have a sales tax license to remit sales tax to the State of Utah nor did it apply for such a license. Neither Olson or Thiokol obtained from the State Tax Commission an exemption certificate or clearance as contemplated under Regulation 58 of the Sales Tax Regulations, but it is conceded that commencing immediately after the execution of said subcontracts in January of 1959, both Olson and Thiokol commenced discussions with the Tax Commission concerning the exemption from sales tax of said sales and on or about March 23, 1959, an informal hearing was held before the Commission. On June 3, 1959, the parties were advised that the Tax Commission had determined that a sales tax should be collected and paid upon said purchases.

Contract Provisions:

The prime contract between Thiokol and the United States provides in Clause 25 that title to all property purchased by the contractor, for the cost of which the contractor is entitled to be reimbursed as a direct item of cost under the contract, shall pass to and vest in the Government upon delivery of such property by the vendor. Said clause further provides that "all personal property for the cost of which the contractor is entitled to be reimbursed hereunder and all other government-owned personal property provided hereunder shall re-

main personalty although affixed to realty not belonging to the Government.”

The contracts entered into between Thiokol and Olson for the construction of the facilities covered thereby provide for partial payments to be made as the work progresses at the end of each calendar month or as soon thereafter as practicable on estimates made or approved by Thiokol. Paragraph 6(a) of the contract states that: “In preparing estimates the material delivered on the site and preparatory work done may be taken into consideration.”

Paragraph 36 of the Thiokol-Olson contracts provide with respect to title as follows: “Title to all property furnished by the Government and/or Thiokol shall remain in the Government and/or Thiokol as applicable. Title to all property purchased by the contractor for use or consumption in the performance of this contract shall pass to and vest in the Government immediately upon delivery to the site, whether delivered by contractor or a third party, or upon payment therefor, whichever first occurs.”

Presumably, as a result of the State Tax Commission Sales Tax Regulation No. 58, the contract between Thiokol and Olson expressly stated that: “Purchase of materials and supplies to be used or consumed in the performance of this contract are exempt from state sales and use taxes. The contractor agrees and certifies that the contract price does not include any amount or contingency for such taxes.”

Sales Tax Act and Regulations:

Section 59-15-2(e), Utah Code Annotated, 1953, defines the term "retailer" to mean "a person doing a regularly organized retail business in tangible personal property, known to the public as such and selling the user or consumer and not for resale. . . ."

Section 59-15-5, which imposes the tax, specifically excludes sales made by a wholesaler to a retailer or in other words a sale for resale.

At the time the contracts in question were entered into Regulation 58, promulgated by the State Tax Commission, read as follows:

"58. Materials and supplies sold to owners, contractors and repairmen of real property. — Such sales may be classified as follows:

I. To owners — sales are taxable — such sales are to final buyers and not for resale;

II. To contractors and subcontractors for use by them in fulfilling contracts for erecting, building on, or otherwise improving, altering or repairing the real property of others:

A. Where the contractor agrees for a lump sum to furnish the materials, supplies and necessary services, the sale to him of the materials and supplies is taxable as he becomes the consumer thereof or final buyer. Cost plus contracts are regarded as lump sum contracts for the purpose of this regulation. The above holding is true regardless of with whom the contract is drawn whether it be a governmental instrumentality or otherwise. In connection with government contracts the following exemptions exist:

1. *Where the contract provides that title to the materials purchased shall vest in the government or instrumentality thereof prior to its use in the construction, the purchase by the contractor shall be deemed a purchase for resale and the contractor shall be required to obtain a sales tax license.*

2. Sales to contractors who are authorized by the United States Government or an instrumentality thereof to make purchases in the name of the government or instrumentality thereof are deemed to be sales to an agent of the United States government or the instrumentality thereof and are, therefore, exempt from tax.

Governmental contractors claiming exemption from any purchases made pursuant to their contract must secure a clearance from the state tax commission prior to making such purchase. Supply houses should collect tax on all sales to contractors unless the contractor gives an exemption certificate which indicates the basis for the claimed exemption and stipulates that proper clearance has been secured from the state tax commission.

B. Where the contractor agrees to furnish the material and supplies at a fixed price or at the regular retail price and to render the services either for an additional agreed price or on the basis of time consumed, the sale to him of materials and supplies is for resale and not subject to the tax. The contractor then becomes the retailer and the sale by him to the owner is a taxable sale. In this event the final buyer is the person whose property is improved, altered or repaired, and the sale is made at the time the contract or job is completed and accepted by the property owner.

In case a contractor enters into both of the above kinds of contracts, he shall be deemed to be a retailer of tangible personal property and shall register with the state tax commission, obtain a sales tax license, purchase all materials for resale and report his liability direct to the state tax commission.

Contractors and repairmen who enter into contracts or repair work of the type referred to herein include such persons as building, electrical, plumbing, paper hanging, sheet metal, bridge, road, landscape, excavating, roofing or similar contracts or repairmen.

Contractors or repairmen in no case should give a resale certificate when they purchase materials, supplies, equipment or other articles for their own use and consumption. Such purchases, which would include fuel, cement mixers, trucks, tractors, or other machinery and equipment, are taxable to the seller thereof.

This regulation is not applicable to contracts whereby the retailer merely agrees to sell and install a complete unit of equipment under conditions whereby such unit may remain a chattel. In such instances the contract will not be regarded as one for improving, altering or repairing real property. For example, the maker of an awning or blinds agrees not only to sell them but to hang them; an electrical shop sells electrical fixtures and agrees to attach them; a dealer sells draperies and window shades and agrees to install them; a retailer sells an oil burner or heating equipment and contracts to install the same; a dealer sells linoleum and agrees to lay it; a cabinet maker sells show cases, counters and cabinets and agrees to install them; a retailer sells a sprinkling system and contracts to install it. A person performing such contracts is primarily a retailer of tangible

personal property and should segregate the full retail selling price of such property from the charge for installation, as the tax applies only to the retail price of the property. If such retailer fails to make such segregation on the customer's invoice, the sales tax applies to the entire contract price including the installation charge. In no case will the retail price be deemed less than such person charges for similar materials and supplies to another installer.

Persons engaged in the foregoing types of business shall register with the state tax commission, obtain a sales tax license and report their liability directly to the state tax commission."

During the course of negotiations in this case and prior to the completion of the subject contracts, Regulation 58 was amended effective July 1, 1959, and the paragraph under II(A) relating to governmental contracts was deleted and subparagraph II(A) was rewritten. The paragraph II(B) was not changed by the amendment.

The new Regulation 58 is not quoted herein but it might be noted in passing that the lettering and numbering of the paragraphs in said Regulation are incomplete and difficult to follow.

STATEMENT OF POINT

POINT I

THE SALES FROM THE VARIOUS VENDORS (INCLUDING EMPIRE AND FIFE) TO OLSON PURSUANT TO ITS CONTRACT WITH THIOKOL WERE PURCHASES BY OLSON FOR PURPOSE OF RESALE AND

WERE THEREFORE EXEMPT FROM UTAH
SALES TAX.

ARGUMENT

POINT I

THE SALES FROM THE VARIOUS VENDORS (INCLUDING EMPIRE AND FIFE) TO OLSON PURSUANT TO ITS CONTRACT WITH THIOKOL WERE PURCHASES BY OLSON FOR PURPOSE OF RESALE AND WERE THEREFORE EXEMPT FROM UTAH SALES TAX.

Effective Contract Provisions:

The provisions of the contracts between Thiokol and Olson are not in dispute. It is clear under paragraph 36 of the contracts that title to all property purchased by Olson passed to and vested in the Government upon delivery to the site. The contract goes to great lengths to make it clear that title to the materials vests in the Government before construction commences. This position is strengthened by the fact that the bid forms required a segregation as between material costs and labor costs. The provisions of paragraph 6 further provide that partial payments can be made on materials that have been delivered to the site even though they have not yet been included in the work performed.

It, therefore, appears clear as between the parties that purchases of materials made by Olson in the performance of its contracts with Thiokol were purchases

made for purpose of resale to the Government and that Olson was, therefore, not the final consumer.

As noted above, the Utah Sales Tax Act specifically excludes from its operation sales which are made for resale as contrasted with retail sales. We have no doubt that the Legislature could enact legislation, as some states have, specifically imposing a tax upon sales made under the circumstances of this case. However, as our sales tax act and regulations now stand, the sales in question are not subject to the tax.

Regulation 58 which was in effect in December of 1958 when the contracts between Olson and Thiokol were entered into specifically provides that:

“Where the contract provides that title to the materials purchased shall vest in the government or instrumentality thereof prior to its use in the construction, the purchase by the contractor shall be deemed a purchase for resale. . . .”

No logical argument can be made that the provisions of the foregoing Regulation are not exactly in point with the circumstances under consideration. However, even if the Tax Commission had the authority to retroactively amend its regulations, the following provision which is still in Regulation 58 would in our opinion be controlling:

“Where the contractor agrees to furnish the material and supplies at a fixed price or at the regular retail price and to render the services either for an additional agreed price or on the basis of time consumed, the sale to him of materials and supplies is for resale and not subject to the tax.”

Olson agreed with Thiokol to furnish the material and supplies required for its bid at a separate price and to render services in the construction of the facilities at a separate price. The contract required that the invoices and requests for payment from Olson to Thiokol separately list and itemize labor and materials as separate items.

The Supreme Court of the State of Utah has never considered the question presented in this case. In the case of *Utah Concrete Products Corp. v. State Tax Commission*, 101 Utah 513, 125 P. 2d 408, the question under consideration was the sale of materials to contractors engaged in construction of state road projects. The contracts involved did not contain the language similar to those in the present case and the Court held under the circumstances that the contractors were consumers and were, therefore, subject to the payment of sales tax.

Other states without the benefit of specific regulations exempting such purchases (as is done by Regulation 58) have concluded that the sales and use tax do not apply to purchases of this type where title to the materials or component parts vest in the Government before construction commences. See *Avco Manufacturing Corporation v. Connelly*, 145 Conn. 161, 14 A. 2d 479 (1958) and *United Aircraft Corporation v. Connelly*, 145 Conn. 176, 140 A. 2d 486 (1958). The Connecticut Supreme Court in these cases held the sales of material to the Government contractor exempt not on the "resale" argument but on the ground that the contractor was not the ultimate consumer in view of the fact that the title vested

in the Government. A similar argument could be made under the laws of our State in view of the other provisions of Regulation 58.

Tax Commission Regulations:

A serious question is presented in this case. It is a question not only having great legal significance but also having broad implications of public policy and an indication of the relationship between State government and private business.

We have confronting us the following picture: In December, 1958, the taxpayers involved in this matter, Thiokol and Olson, entered into contracts for the construction of certain facilities. The Sales Tax statutes did not specifically define the term "sale for resale." At that time the Regulations of the Tax Commission stated very clearly and succinctly that purchases made by Olson under such contracts were exempt from Sales Tax. The parties expressly so provided in their contracts. Work immediately commenced under the contracts and purchases were made by Olson. The question of exemption from Sales Tax immediately arose and within a month discussions commenced with the Tax Commission. Thereafter, before performance was completed under the contracts the Tax Commission amended its regulations and then sought to apply the amended regulations to the transaction in question.

One might ask whether as a matter of public policy this presents a picture of which the State of Utah can be proud. Does this create a climate which is attractive

to outside business interests seeking an area in which to expand? These questions might be considered in the light of the fact that many states, such as California, have elected to pass specific legislation exempting sales of the nature involved here from the application of sales and use taxes.

Under Section 59-15-20, the State Tax Commission is given authority to "prescribe forms and rules and regulations in conformity with this Act for the making of returns and for the ascertainment, assessment and collection of the taxes imposed hereunder." Under this section, the Commission does not have authority to vary the language of the Act or to include taxpayers who are not designated by the Act. *Western Leather & Finding Co. v. State Tax Commission*, 87 Utah 227, 48 P. 2d 526.

But where there is uncertainty as to a particular transaction, the construction of the Commission can be very important, particularly as a guide to taxpayers as well as the courts. The Supreme Court in *E. C. Olsen Co. v. State Tax Commission*, 109 Utah 563, 168 P. 2d 324, observed:

"Where there is an ambiguity in the statute as to whether the latter does or does not cover a particular matter, a practical construction of the statute shown to have been the accepted construction of the agency charged with administering the matters in question under the statute will be one factor which the court may take into consideration as persuasive as to the meaning of the statute."

The above case involved only an informal oral statement made by a Tax Commission Auditor and the acquiescence of the Commission over a period of time. Certainly a formal, published regulation such as Regulation 58, in effect for several years, should be given even more than persuasive effect when it is amended while a controversy is under discussion.

The Supreme Court of this State has not considered the effect of amendments to Commission regulations and whether or not such amendments may be applied retroactively. It is clear under our statutes that the Commission does not have express authority to make its amendatory regulations retroactive in their effect.

Professor Griswold in his discussion of this subject suggests that while a regulation may be freely and retroactively amendable in its early and formative days, that it should not be so amendable, particularly against the interest of an individual, after it has been in effect for several years and become "seasoned." 54 Harvard Law Review 413. Many of the recent Federal statutes contain express provisions protecting an individual from liability for acts done or omitted in conformity with administrative rules or regulations, notwithstanding the fact that such rule or regulation may be thereafter amended. See for example, Securities Exchange Act of 1934, 15 U. S. C. §78(w) (a) and Securities Act of 1933, 15 U. S. C. §77s(a).

In the absence of specific legislation restricting the retroactive application of regulations the same result has still been reached in numerous federal cases. In *National*

Labor Relations Board v. Guy F. Atkinson Co., 195 F. 2d 141 (9th Cir. 1952), we find the following statement:

“We think it apparent that the practical operation of the Board’s change of policy, when incorporated in the order now before us, is to work hardship upon respondent altogether out of proportion to the public ends to be accomplished. The inequity of such an impact of retroactive policy making upon a respondent innocent of any conscious violation of the Act and who was unable to know, when it acted, that it was guilty of any misconduct of which the Board would take cognizance, is manifest. *It is the sort of thing our system of law abhors.*” (Emphasis added)

One of the leading cases holding that Treasury Regulations may not be retroactively applied, particularly where Congress has re-enacted the statute involved while the original regulation was in effect, is *Helvering v. R. J. Reynolds Tobacco Co.*, 306 U. S. 110, 59 Sup. Ct. 423 (1939).

In some states it has been held that where regulations are formally promulgated by an administrative agency, it may not thereafter seek to disregard or repudiate them. *Springborg v. Wilson and Company*, 73 N.W. 2d 433, 435 (Minn. 1955).

It is not unusual to find a taxpayer contending that the Tax Commission’s regulations do not correctly state or interpret the law. It is a unique situation to find the Tax Commission itself seeking to avoid the plain language and effect of its own regulations.

The Tax Commission has argued that its regulation was void and contrary to law because of the decision of this Court in *Utah Concrete Products Corporation v. State Tax Commission*, 101 Utah 513, 125 P. 2d 408. This case held under the facts involved that the contractor was the consumer, but completely different contract provisions and circumstances were involved. It also seems odd that if the Tax Commission felt the decision in the *Utah Concrete Products* case voided its regulation and made it contrary to law that they waited from April 25, 1942, when the latter case was decided until July 1, 1959, when the Thiokol problem was before them, before amending its regulation.

CONCLUSION

Petitioners are entitled to a refund of the sales tax paid by Olson to its various vendors (including Fife and Empire) in the performance of its contracts with Thiokol. It has been conclusively shown that the provisions in said contracts vested title in the Government to all materials and supplies purchased by Olson immediately upon delivery at the site and prior to use and/or consumption in the performance of the contracts; that the parties clearly intended that the purchases should be for "resale" to the Government as evidenced by a fixed price for all such items established by a breakdown of material costs submitted by the contractor with its bid and the further requirement that the contractor separately account for and invoice the materials and supplies; and that such purchases qualify for exemption from Utah Sales and Use

Taxes as purchases for "resale" under the proper interpretation of the statutes and regulations. This result is inescapable under (1) the provisions of Regulation 58 as said regulation existed at the time the contracts were entered into and when many of the purchases were made, and (2) the provisions of the Sales Tax Act regardless of the repeal of Regulation 58.

Respectfully submitted,

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