1983

Institutional Laundry, Inc. v. Utah State Tax Commission : Appellant's Brief

IN THE SUPREME COURT OF THE STATE OF UTAH

INSTITUTIONAL LAUNDRY, INC., Petitioner-Appellant,	)	Case No. 19390
v.	)	
UTAH STATE TAX COMMISSION, Respondent.	)	

APPELLANT'S BRIEF

Appeal from the Third Judicial Court of Salt Lake County

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Statement of the Nature of the Case

This case involves a controversy as to liability for sales taxes in the sum of $9,637.87, plus interest, on the nonprofit services rendered by petitioner and appellant to its parent corporation during the period from July 1, 1978 through December 31, 1979.

Disposition of the Case in the Lower Court

The district court, on cross-motions for summary judgment by both parties, granted summary judgment for respondent and thereby affirmed the assessment of sales taxes made by the Utah State Tax Commission.

Nature of the Relief Sought on Appeal

By this appeal petitioner and appellant seeks to have the assessment of sales taxes against it set aside in its

entirety, or at least to the extent of seventy-three percent of that assessment, the percentage of petitioner's services attributable to Medicare and Medicaid patients.

Statement of Facts

Petitioner was a Utah corporation duly qualified to do business in the State of Utah from July 1, 1978 through December 31, 1979, the period of time in issue in this case. During that period petitioner was a wholly-owned subsidiary of Wasatch Medical Management Services, Inc. ("WMMS"). Petitioner provided only laundry services for WMMS, which were provided on a nonprofit basis. Those services were the only business of petitioner.

Petitioner existed only for the administrative convenience of WMMS. It owned no property. Its books were kept by WMMS, and the boards of directors of both corporations were the same. No separate board meetings were held for petitioner, and no separate minutes were kept. Petitioner is now a division of WMMS and has no separate corporate existence.

For the period in question seventy-three percent of petitioner's services were provided for Medicare and Medicaid patients, for which services petitioner was reimbursed from public funds in accordance with applicable Medicare and Medicaid guidelines, on a nonprofit basis. WMMS is now, and was during the period in question, a health care provider. State and federal Medicare and Medicaid guidelines prohibit, and did prohibit during the period in question, the making of a profit by a company such as petitioner related to a health care provider

such as WMMS. Any sales taxes assessable to petitioner on services rendered by it to WMMS for Medicare and Medicaid patients would be reimbursable from Medicare and Medicaid funds.

Respondent assessed sales taxes in the amount of $9,637.87 on nonprofit services rendered by petitioner to WMMS for the period in question, plus interest. Petitioner appealed that assessment to respondent through a formal hearing, following which respondent issued a written decision on March 8, 1982 affirming the assessment of sales taxes on petitioner and ordering petitioner to pay it.

All of the facts stated above were alleged by petitioner in its petition before the district court and were admitted by respondent. Petition filed April 7, 1982 and Answer dated May 6, 1982. On cross-motions for summary judgment by the parties, the district court issued its final order granting respondent's motion for summary judgment based on the facts stated above, denying petitioner's motion for summary judgment, and entering judgment for respondent.

ARGUMENT

I. Petitioner Should be Relieved of any Sales Tax Liability.

No sales tax liability should be imposed on petitioner, due to its transparent and temporary existence. Respondent has imposed sales tax liability on petitioner for its nonprofit services that were rendered solely to its parent corporation, during a period when petitioner was technically a separate corporation but in substance had no separate existence. If

Institutional Laundry had been a division of its parent corporation, as it now is, its services would undoubtedly be nontaxable.

During the period petitioner was a separate corporation from its parent and was subjected to sales tax liability by respondent, no corporate formalities were observed. The laundry services petitioner provided for its parent corporation were petitioner's only business and were provided on a nonprofit basis. Petitioner existed only for the administrative convenience of its parent. It owned no property, its books were kept by its parent corporation, and the boards of directors of both corporations were the same. No separate board meetings were held for petitioner, and no separate minutes were kept. Petition, ¶¶2,3.

Under similarly compelling facts, the court in Mapo, Inc. v. State Board of Equalization, 53 Cal. App. 3d 245, 125 Cal. Rptr. 727 (1975), held that a subsidiary corporation could not be separately taxed on sales to its corporate grandparent, Walt Disney Productions. The plaintiff's sole function was to fabricate entertainment devices, chiefly animated mechanical figures, for use at Disney amusement parks. It existed as a separate corporation for only six years, at which time it became a division of its parent corporation. It acted solely on orders from its grandparent corporation and existed as a separate entity only to make fabrication of items possible by reaching agreements with a single vertical labor union.

While recognizing the general rule that courts should not disregard separate legal entities merely to grant relief from taxation, the court held that the insubstantiality of the subsidiary corporation, and its identity with its parent and grandparent corporations, were such that sales taxes were not assessable on its operations. The court explained (125 Cal. Rptr. at 730):

> "Mapo appeared, simplified these union negotiations, acted as conduit for payment of salaries for certin Prodution personnel, and disappeared without noticeable effect. The temporary, paperwork transactions which resulted from its existence did not justify the imposition of sales taxes intended for dealings between separate producers and consumers.
>
> ". . . . We think the Board ignores substance for form." (Emphasis added.)

The rationale of the Mapo case is directly applicable to the present case. Institutional Laundry existed as a separate corporation only for a very limited time, strictly for administrative convenience, and without corporate substance. Its services rendered solely to its parent corporation on a nonprofit basis ought not to be taxed.

II. Petitioner is not Liable for any Sales Tax Attributable to Services for Medicare or Medicaid Patients.

Seventy-three percent of Institutional Laundry's

services were provided for Medicare and Medicaid patients during the period in question, and for those services it was reimbursed from public funds in accordance with applicable Medicare and Medicaid guidelines, on a nonprofit basis. Petition, ¶4. Not only were such services provided on a nonprofit basis, but applicable Medicare and Medicaid guidelines prohibited such services from being provided other than on a nonprofit basis. Petition, ¶5. Any sales taxes that Institutional Laundry might be required to pay, relating to Medicare and Medicaid patients, would itself be reimbursable from public funds. Petition, ¶6. The imposition of such tax liability would therefore result in no net collections to the public treasury but would only add to the administrative burden on plaintiff and also on state and federal health care agencies.

In the case of Ogden Union Railway and Depot Co. v. State Tax Commission, 16 Utah 2d 23, 395 P.2d 57 (1964), modified on other grounds, 16 Utah 2d 255, 399 P.2d 145 (1965), this Court held that a subsidiary corporation could not escape sales tax liability on services rendered for its parent corporations, even though such services were rendered on a nonprofit basis, for there was no prohibition against the taxpayer corporation making a profit. In accordance with decisions in other jurisdictions, this Court held that where a profit was permitted to be made it was immaterial whether there actually was a profit, so long as the transactions conferred or were intended to confer a benefit or advantage to the parties involved.

This Court distinguished a decision of the Illinois Supreme Court that held sales taxes were not assessable on services rendered by a subsidiary corporation to its parent on a nonprofit basis where profits were prohibited:

> "In Valier Coal Co. v. Dept. of Revenue, 11 Ill.2d 402, 143 N.E.2d 35, 64 A.L.R.2d 763 (1957), the plaintiff was a subsidiary corporation formed for the purpose of providing coal on a nonprofit basis to the parent corporations, the Burlington and Quincy Railroads, pursuant to an order of the Public Utilities Commission. There the court defined business in the 'commercial sense' indispensable to which is the profit element. The Minnesota Supreme Court correctly distinguishes this case as not being authority for the nonprofit principle because '. . . the revenue department could not impose a tax on the subsidiary for doing something that it had been prevented from doing by the utilities commission.' State v. Minneapolis & St. Louis Ry. Co. (Minn.) 100 N.W.2d 669, 677 (1959)." (16 Utah 2d at 27-28.) (Emphasis added.)

This Court also found untenable the taxpayer's argument that its business was not taxable because it was limited to

serving its parent corporations. It again distinguished the Valier Coal case, as follows (16 U.2d at 28):

> "If the order had come from a state agency ordering plaintiff to provide nonprofit services, then the Valier Coal argument would be more persuasive." (Emphasis added.)

The Ogden Railway case thus indicates the applicability of the Valier Coal case to a situation where a subsidiary corporation, in rendering services to its parent, not only makes no profit but is prevented from doing so. In the Valier Coal case, supra, the State of Illinois assessed a sales tax on sales of coal by the taxpayer to its parent corporation on a nonprofit basis. The Illinois Supreme Court annulled the assessment because the operations of the taxpayer had been limited, by an order of the Illinois Public Utilities Commission, to sales only to its parent and at a price not to exceed its actual production costs. The court held that no tax was payable under these circumstances, reasoning that "it would be anomalous, if not inequitable" for the state, on the one hand, to limit the taxpayer's operations for the public good and then, on the other hand, to hold that such limited operations constituted a taxable business. (143 N.E.2d at 39.)

Institutional Laundry was similarly prevented from operating at a profit by state and federal regulations (Petition, ¶5) and should likewise be exempt from sales taxes to the extent its services were rendered for Medicare and Medicaid patients.

Petitioner is not liable for any sales tax on its services that were provided for such purposes.

III. Conclusion.

Petitioner respectfully submits that the sales tax assessment should be set aside in its entirety. At the least, seventy-three percent of the assessment, the portion attributable to services for Medicare and Medicaid patients, should be set aside, since those services were prohibited by federal and state regulation from being provided on a profit basis.

Date: October 13, 1983

Respectfully submitted,

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Certificate of Mailing

I hereby certify that I mailed a copy of the foregoing Appellant's Brief to David L. Wilkinson, Attorney General, Stephen G. Schwendiman, Assistant Attorney General, Frank V. Nelson, Assistant Attorney General, 124 State Capitol, Salt Lake City, Utah 84114, the attorneys for respondent, by placing a copy thereof in the United States mail, postage prepaid, this fourteenth day of October, 1983.

Julie Ann Lawson