

IN THE DISTRICT COURT OF LANCASTER COUNTY, NEBRASKA

TODCO BARRICADE COMPANY,

Plaintiff,

v.

DEPARTMENT OF REVENUE,

Defendant.

) Docket 505

Page 256

) Dept. of Justice

) ORDER JUL 25 1994

) State of Nebraska

)

This is an appeal, pursuant to NEB. REV. STAT. § 77-27,127 (Reissue 1990) and § 84-917 (Cum. Supp. 1992) from an Order of the State Tax Commissioner [the Commissioner] dated October 18, 1993, denying a claim for refund of Nebraska sales tax in the amount of \$42,456.33, made by Todco Barricade Company [Todco], for the tax periods between April 1, 1990, and March 31, 1993. Review is conducted by the court, without a jury, de novo on the record presented at the hearing held by the Nebraska Department of Revenue [the Department]. NEB. REV. STAT. § 84-917(5)(a) (Cum. Supp. 1992).

FACTS

Generally speaking, the court adopts the facts set forth in the Commissioner's Order of October 18, 1993; however, as a backdrop, some facts are recited herein.

Todco has its principal place of business in Omaha. It is a supplier, renter/lessor, seller and subcontractor of highway safety devices. Its subcontracts involve the subcontracting of labor, barricades, arrow boards, high intensity lights, sign installations, temporary pavement marking and other specified items to general contractors constructing roads for Nebraska governmental bodies. The transactions covered by Todco's refund claim involve subcontracts where Todco supplied Type III barricades, arrow boards and Type B high intensity lights [hereinafter referred to at

times as the property furnished by Todco] to general contractors performing road or bridge construction projects for the State of Nebraska, through the Department of Roads or for other governmental units (such as counties, cities or other political subdivisions).

The contracting process began when the governmental unit would determine that a road or bridge construction project was needed and would, then, develop plans, specifications, drawings, general and special provisions and other documents which detailed the project's requirements. As a part of those requirements, the governmental unit would establish elaborate and detailed plans for barricade, arrow board and high intensity light requirements on the project site.

General contractors subcontracted with Todco to supply the barricades, arrow boards and high intensity lights required by the governmental units on the project sites. Todco's subcontracts, by reference, included all of the general and special conditions, drawings, plans, specifications, manuals, standard and site specific traffic control plans, addenda and other documents made a part of the contract between the governmental unit and the general contractor. Todco, in accordance with its subcontract, was required to follow the plans, specifications and other directions developed by the governmental unit with regard to the barricades, arrow boards and high intensity lights. Failure by Todco to comply with the project requirements issued by the governmental unit constituted a violation of the subcontract.

The exact number, placement and timing of placement and movement and removal of barricades, arrow boards and high intensity lights were determined by the governmental unit, first as indicated in the project plans and specifications and then as adjusted by the on-site project

manager or engineer. If variances or deviations from the standard traffic control plan were necessary, the project manager would take the guidelines in the standard traffic control plans and develop a site-specific traffic control plan indicating the exact number and placement of the barricades, arrow boards and/or high intensity lights, as well as the exact number and placement of any subsidiary items. Variances and deviations regarding type, number, placement or timing would occur only at the request or with the approval of the project manager or engineer.

To be awarded a subcontract, Todco would place a bid with a general contractor. In the calculation of its bid price, Todco determined the various cost elements it would have in meeting the subcontract, including the equipment, labor, subsidiary items needed on the project, insurance, repair expense, office expense, fuel, truck expense and other factors. Todco would then make its bid to provide the barricades, arrow boards and high intensity lights required by the project plans and specifications. The property to be furnished by Todco was bid on a per unit per day basis. That per unit per day price would remain fixed, regardless of the number of units per day actually used on the project site. Payment by the general contractor to Todco, which was made monthly, would not be affected by the amount of labor or other variations required to comply with the barricade, arrow boards and high intensity light subcontracts requirements.

The barricades, arrow boards and high intensity lights were placed by Todco on the projects and remained there until the project was completed, unless movement was required according to the plans and specifications or directions from the contractor or they became unnecessary under the plans and specifications. Generally, barricades

and/or arrow boards would be placed and not moved again for extended periods of time. Projects could require more frequent movement of barricades under certain conditions, such as ramp closures and openings to accommodate heavy local traffic. The governmental unit in those instances would require that barricades and arrow boards be placed by a certain time of the day and then removed by a later time of the day to help direct and control traffic.

Under the subcontracts, Todco would provide the labor and trucks necessary to comply with these requirements. Following completion of a phase of the project, or of the project itself, Todco would move the barricades, arrow boards and high intensity lights either to the next phase of the project, as indicated by the general contractor, or off the project site, if they were no longer required. At any time, Todco could replace or substitute the barricades, arrow boards, or high intensity lights, as they needed repair or became unnecessary under the project requirements, but its subcontracts required that Todco, at all time, provide the types, number and placement of barricades, arrow boards and high intensity lights in accordance with the governmental unit's requirements. Todco did not maintain a continuous presence on any project site and could be absent from a project site while barricades, arrow boards and high intensity lights were in place for up to one week.

ISSUES

1. Whether the subcontracts between Todco and its general contractors constituted a rental or lease of tangible personal property and, therefore, was subject to sale tax under the Nebraska Revenue Act of 1967 and amendments thereto.
2. Whether Todco was exempt from sales tax as an "operator" of barricades, arrow boards or high intensity lights, as discussed in Nebraska Department of Revenue Regulations.

DISCUSSION

The State of Nebraska imposes a tax on the gross receipts of all sales of tangible personal property. NEB. REV. STAT. § 77-2703(1) (Supp. 1993). Included within the definition of "sale" are leases and rentals. NEB. REV. STAT. § 77-2702.15 (Supp. 1993). Gross receipts is defined in NEB. REV. STAT. § 77-2702.07(1) (Supp. 1993) to include the total amount of the lease or rental price. Specifically, rental or lease price includes ". . . the total amount for which property is rented or leased, . . . without any deduction on account of . . . labor or service cost The total amount for which property is rented or leased shall include any services which are a part of the lease or rental" NEB. REV. STAT. § 77-2702.12 (Supp. 1993). Therefore, if the subcontracts between Todco and its general contractors constituted leases or rentals of tangible personal property, they were properly subject to sales tax.

The Nebraska legislature has not defined the term "lease" within the context of the Nebraska Revenue Act of 1967. NEB. REV. STAT. §§ 77-2701 through -77,135 (Reissue 1990, as amended). When words or phrases are undefined, they are to be given their ordinary meaning. *State Bd. of Agriculture v. State Racing Comm'n.*, 239 Neb. 762, 478 N.W.2d 270 (1992).

BLACK'S LAW DICTIONARY 889 (6th ed. 1990) defines "lease," when related to tangible personal property, to mean

. . . a contract by which one owning such property grants to another the right to possess, use and enjoy it for specified period of time in exchange for periodic payment of a stipulated price, referred to as rent. [Citation omitted].

Application of this definition leads to the conclusion that the subcontracts between Todco and its general contractors constituted leases subject to taxation.

First, tangible personal property was involved; second, contracts were entered into in the form of subcontracts; and, third, periodic payments were made to Todco by its general contractors. The remaining element to be determined is whether the general contractors obtained possession, use and enjoyment of the property furnished by Todco.

"Use" is defined in NEB. REV. STAT. § 77-2702.23(1) (Supp. 1993) to mean ". . . the exercise of any right or power over property incident to the ownership or possession of that property . . ."

Under the facts of this case, the general contractors enjoyed the exercise of rights over the property furnished by Todco. First, the general contractors used the property to comply with governmental unit contract specifications. Those specifications set forth the location, number and type of property needed, as well as the time frame in which the property was to be utilized by the general contractors. Second, the general contractors used the property to protect its workers and the general public and to provide traffic control. In addition to their right to use the property furnished by Todco, the general contractors also needed to acquire the right to possess the property in order for a lease to exist.

Although not defined by statute, "possession" is defined in BLACK'S LAW DICTIONARY 1163 (6th ed. 1990) as:

The detention and control, or the manual or ideal custody, of anything which may be the subject of property, for one's use and enjoyment, either as owner or as the proprietor of a qualified right in it, and either held personally or by another who exercises it in one's place and name.

Whether a person has possession of an item, therefore, is a question of control. BLACK'S LAW DICTIONARY 329 (6th ed. 1990) defines "control" as:

Power or authority to manage, direct, superintend, restrict, regulate, govern, administer, or oversee. The ability to

exercise a restraining or directing influence over something.
[Citation omitted].

It is evident from the facts, that the general contractors exercised control over the property furnished by Todco. The exact number, type, location and time for placement and removal of the property was specified by a project plan, over which Todco had no control. In order for Todco to make any variances from these specifications, it first had to gain approval from the individual general contractor, who was then required to seek approval from the project manager or engineer. The general contractors would contact Todco when it was time to move or replace property. The general contractors would also contact Todco for replacement or repositioning, if a piece of property was knocked down; although, in emergency situations, a general contractor's employees would restand a piece of property knocked down.

Providing maintenance and repair does not constitute control by Todco over the property it furnished. Todco's ability to determine the manner and method of transportation and its setting up and removal of the furnished property is likewise insufficient. Todco had no discretion regarding the type of property to be transported or to where the property was to be transported. In this regard, Todco was only following set specifications. In fact, a standard provision in Todco's subcontracts stated that Todco was responsible to the general contractors and was required to follow all directions and instructions regarding the property furnished.

Todco points to *State v. Steel City Crane Rental, Inc.*, 345 So.2d 1371 (Ala. Civ. App. 1977), to support its argument that a lease did not exist between Todco and its general contractors. In *Steel City*, the court found that the furnishing of cranes and operators did not constitute a lease, because the crane owners maintained control and possession of the cranes.

Id. at 1373. Unlike the present case, however, the crane owners in *Steel City* determined the type of crane to be used for a project, as well as where and how the crane was to be operated. *Id.* at 1372 and 1374. Additionally, the cranes were under the physical control of the owner's employee (i.e., the operator) at all times. *Id.* at 1372. *See also, City of Phoenix v. Bentley-Dille Gradall Rentals, Inc.*, 665 P.2d 1011 (Ariz. App. 1983) (owner had possession and control of equipment, where its employees retained physical control over the equipment at all times and the owner determined the size of equipment necessary to complete the job).

Todco has demonstrated no similar control, since it was allowed no discretion regarding the type, number or location of the property used on a project site. Further, Todco did not establish plans or techniques, but, rather, followed specific plans from which it had no authority to deviate, without authority. Because the general contractors maintained control of the property furnished and the right to use and possess that property, a lease existed between Todco and its general contractors subject to sales tax.

The next issue raised relates to the applicability of various regulations of the Department. Reg. 1-018.03 (Reissue 1986) provided:

All transactions for the use of equipment and operator are presumed rental subject to tax. This presumption may only be rebutted by the taxpayer placing sufficient facts in evidence to show that the transaction is not a transfer of the right to use or direct the use of equipment, but rather is a legally enforceable contract which sets out with definiteness and certainty the terms by which the parties intend to be bound. Facts to be considered would include the following:

018.03A. Establishment of job specifications so as to demand a particular level of performance.

018.03B. Fixed consideration.

018.03C. Control by the lessor of manner, means, and method of performance of a job.

The plain language of this regulation establishes that it was not applicable to this case, since Todco did not furnish equipment with an operator. The Department interprets "operator" to be ". . . a person who has to interact with or manipulate the equipment on an ongoing basis to allow the equipment to perform its function". The property furnished by Todco, once placed by Todco, performed its function of protecting workers and the general public and directing traffic without, generally, the presence of Todco's employees, except for maintenance purposes. This is further evidenced by the fact that Todco's employees were able to be absent from a project site for as long as a week at a time.

Todco argues that the language requiring "an operator" was merely surplusage, because the real focus of the regulation was on the possession aspect of the transaction. Todco argues, further, that the regulation was in excess of the Department's statutory authority, since the Nebraska sales tax statutes speak in terms of possession only, without regard to whether there is an operator present.

Todco correctly identifies possession as the focus of the regulation. Contrary to Todco's argument, however, the Department's regulation was consistent with this focus, as it merely recognized that the presence of an operator with equipment is indicative of control and possession. A further examination of the regulation makes this clear.

Reg. 1-018.03 (Reissue 1986) created a rebuttable presumption that transactions involving the use of equipment and an operator created a lease subject to tax. Because the presence of an owner employed operator

often indicated that, in fact, control and possession did not transfer to the customer, regulations proceeded to list factors which would and would not rebut this presumption. Reg. 1-018.04 (Reissue 1986) provided that a lease existed where the customer (lessee) had the right to direct the manner in which the equipment was used; while Reg. 1-018.05 (Reissue 1986) stated that a lease did not exist where the owner (lessor) retained exclusive control of the manner, means and method of job performance.

Common sense, however, indicates that supplying an operator with equipment makes it more likely than not that the lessor maintains control over the equipment, therefore, negating the existence of a lease. Recognizing this, the regulations issued in 1993 eliminated the rebuttable presumption. *See* 1-018.03 (Reissue 1993).

Clearly, in addressing the applicable regulations, the issue remains possession and control. If the court disregards the "operator" language of the 1986 regulations as surplusage, as Todco requests, the result is the same. Todco did not retain exclusive control of the jobs covered by its subcontracts, as required by Reg. 1-018.05(C) (Reissue 1986). By using the "operator" language, the regulations merely recognized that where an operator is not provided, retention of control by the equipment owner is highly unlikely.

Similarly, Reg. 1-018.07 (Reissue 1986) used the language "with an operator" recognizing that, in order for equipment to be incidental to services rendered, the services rendered must have been substantial, or the "true object" of the transaction. The "true object" of the property furnished by Todco was to provide protection to workers and the general public and to control traffic. The property furnished by Todco independently performed that function. Consequently, transporting and

maintaining the property so that it could perform that function was incidental to the property's primary purpose. *See e.g., Bar Master, Inc. v. State Board of Equalization*, 135 Cal. Rptr. 272 (Cal. Ct. App. 1976) (where beverage dispensing units were obtained for use in making drinks, true object of transaction was functional unit while maintenance and repairs provided by owner were merely incidental) and *Recording Devices Co., v. Porterfield*, 283 N.E.2d 626 (Ohio 1972) (where device makes record of who is unlocking door, the service of picking up and decoding this record is incidental to function provided by device itself).

Todco was not an exempt "operator" under the regulations. In addition, the Department did not exceed its statutory authority in drafting the regulations, since their meaning is consistent with the Nebraska Revenue Act of 1967.

CONCLUSION

For the reasons set forth herein, the decision of the Commissioner, dated October 18, 1993, is affirmed. The costs of this action are taxed to Todco.

A copy of this Order is sent to counsel of record.

Dated July 22, 1994.

SO ORDERED.

BY THE COURT:



Paul D. Merritt, Jr.
District Judge