IN THE DISTRICT COURT OF LANCASTER COUNTY, NEBRASKA

LIVINGSTON ENTERPRISES, INC., a Nebraska corporation, Petitioner, vs. NEBRASKA DEPARTMENT OF REVENUE, an agency of the State of Nebraska, and TONY FULTON, Tax Commissioner, Respondents.	)	CASE NO. CI 16-2027 ORDER

INTRODUCTION

This matter came on for hearing on the merits on October 19, 2016, on the appeal of the Petitioner Livingston Enterprises, Inc. (Livingston), from the May 11, 2016 decision of Tony Fulton, Tax Commissioner of the State of Nebraska (Tax Commissioner), and the Nebraska Department of Revenue (the Department), denying Livingston's claim for a refund of sales tax. Gretchen McGill and Brenda Smith appeared for Petitioner. Assistant Attorney General L. Jay Bartel appeared for Respondents. The court heard arguments, received the transcript of the proceedings, and the matter was submitted. The court, being fully advised, finds and orders as follows.

BACKGROUND

This is an appeal pursuant to NEB. REV. STAT. §§ 77-2708(2)(f) (Cum. Supp. 2014), 77-27,127 (Reissue 2009), and 84-917 (Cum. Supp. 2010) from a final decision of the Department and Tax Commissioner denying a claim for refund of sales taxes filed by Livingston in the amount of $32,478.80.

Livingston is a Nebraska corporation engaged in the business of swine production. In March of 2015, Livingston experienced a devastating fire that destroyed or damaged buildings used to house and care for pigs. Livingston hired Bob Jurgens Construction, Inc. (Jurgens) as a general contractor to construct new buildings and repair damaged buildings. From April through November of 2015, Jurgens purchased concrete hog slats/gang slats (hog slats) from Wahoo Concrete Products (WCP). (T5-55). Jurgens paid WCP a total of $652,372.10 for the hogs slats, which included sales tax in the amount of $32,478.80. (T5, 14). WCP remitted the sales tax paid by Jurgens to the Department. (T2). Livingston fully reimbursed Jurgens for its purchase of the hog slats, including the amount of sales tax Jurgens paid. (T4).

On January 25, 2016, WCP sent a letter to Jurgens which explained that the Department had stated in an email to WCP that the hog slats qualified for a sales tax exemption. (T2-3). On February 4, 2016, Livingston filed a tax refund claim on the basis of the agricultural machinery or equipment exemption, as defined under NEB. REV. STAT. §§ 77-2708.01, 77-2704.36, and 316 N.A.C. § 1-094. (T1). Livingston submitted its claim using Form 7 AG-1, which states that "[c]oncrete hog slats/gang slats" qualify for the agricultural machinery or equipment sales tax exemption. (T64). On May 11, 2016, the Department denied Livingston's refund claim. (T63). The basis for the Department's denial was that the hog slats were not agricultural machinery or

equipment, but instead were building materials which "become an integral part of the building once installed since the concrete slats effectively become the floor of the building." (T61). No administrative hearing was held. Petitioner timely appealed the Tax Commissioner's decision.

STANDARD OF REVIEW

The Tax Commissioner's action on a sales tax refund claim "shall be final unless the taxpayer seeks review of the Tax Commissioner's determination as provided in section 77-27,127." NEB. REV. STAT. § 77-2708(2)(f). "Any final action of the Tax Commissioner may be appealed, and the appeal shall be in accordance with the Administrative Procedure Act." NEB. REV. STAT. § 77-27,127. Under the Administrative Procedure Act, the Court reviews the Commissioner's final decision "without a jury de novo on the record of the agency." NEB. REV. STAT. § 84-917(5)(a).

In a review de novo on the record, the district court is required to make independent factual determinations based upon the record, and the court reaches its own independent conclusions with respect to the matters at issue. *Schwarting v. Nebraska Liquor Control Comm'n*, 271 Neb. 346, 351, 711 N.W.2d 556, 561 (2006). "[T]he presumption under Nebraska law is that the agency's decision was correct, with the burden of proof upon the party challenging the agency's actions." *Gridiron Management Group v. Travelers Indemnity Company*, 286 Neb. 901, 906, 839 N.W.2d 324, 329 (2013). The district court may affirm, reverse, or modify the decision of the agency or remand the case for further proceedings. NEB. REV. STAT. § 84-917(6)(b).

"To the extent the interpretation of statutes and regulations is involved, questions of law

are presented, in connection with which an appellate court has an obligation to reach an independent conclusion irrespective of the decision made below, according deference to an agency's interpretation of its own regulations, unless plainly erroneous or inconsistent." *Utelcom, Inc. v. Egr*, 264 Neb. 1004, 1007, 653 N.W.2d 846, 850 (2002). "[T]ax exemption provisions are to be strictly construed, and their operation will not be extended by construction." *Metropolitan Utilities Dist. v. Balka*, 252 Neb. 172, 176, 560 N.W.2d 795, 799 (1997).

ANALYSIS

The Nebraska Revenue Act of 1967 (the Act) imposes a sales tax on retail sales of tangible personal property sold in this state. NEB. REV. STAT. § 77-2703(1). "This tax is not upon the article sold, but upon the transaction called the sale." 316 N.A.C. § 001.02; *see Anthony, Inc. v. City of Omaha*, 283 Neb. 868, 877, 813 N.W.2d 467, 476 (2012) (a sales tax is "a tax upon *the privilege of buying* tangible personal property") (emphasis added). "The tax imposed by [§ 77-2703(1)] shall be collected by the retailer from the consumer." NEB. REV. STAT.§ 77-2703(1)(a). "The tax required to be collected by the retailer from the consumer constitutes a debt owed by the retailer to this state." NEB. REV. STAT. § 77-2703(1)(a). Pursuant to the Nebraska sales tax scheme, the purchaser must pay the tax on the cost of his or her purchase to the retailer, who must then hold the money in trust before remitting the tax to the state. *Governors of the Knights of Ak-Sar-Ben v. Dep't of Revenue* , 217 Neb. 518, 520, 349 N.W.2d 385, 386-87 (1984). "[F]or the purposes of the sales tax statutes the purchaser ... is the taxpayer. *Id.* at 520, 349 N.W.2d at 387. "The legal incidence of a sales tax falls upon the purchaser." *Anthony, Inc. v. City of Omaha*, 283 Neb. at 878, 813 N.W.2d at 476. Per Nebraska

statutes and case law, the retailer does not pay the tax, but is instead responsible for collecting and remitting sales tax paid by the purchaser.

The Act provides certain sales tax exemptions based on the status of the purchaser or the type of property sold. *See, e.g.*, NEB. REV. STAT. §§ 77-2704.07 to 77-2704.43. The sales tax exemption at issue in this case is the agricultural machinery or equipment exemption, which provides: "[a]ny purchaser of depreciable repairs or parts for agricultural machinery or equipment used in commercial agriculture may apply for a refund of all of the Nebraska sales or use taxes ...." Under the Department Regulations, "agricultural machinery and equipment" is defined as "tangible personal property that is used directly in the cultivating or harvesting a crop, *the raising and caring for animal life*, or the collecting or processing of an agricultural product on the farm or ranch." 316 N.A.C. § 094.01(A) (emphasis added). In denying Petitioner's claim for refund, the Department determined the hog slats were not tangible personal property, as contemplated by the exemption, but instead constituted "building materials." "Building materials" are defined as "any property, including fixtures, that will be annexed to the land or an improvement on the land." 316 N.A.C. § 1-017.02C. The Department concluded the hog slats were annexed to Livingston's real property and "effectively [became] the floor of the building." (T63).

On appeal, Livingston argues the Department and the Tax Commissioner erred in concluding Livingston is not entitled to a sales tax refund, because the hog slats are used directly in the raising and caring for pigs. Livingston points out the Department's 7AG-1 Form explicitly includes hog slats as an item that is exempt from sales tax. In response, the Department and the Tax Commissioner cite to *Iowa Ag Constr. Co. v. Iowa Bd. of Tax Review*, 723 N.W.2d 167 (Iowa 2006) to support their interpretation that the hog slats became annexed to real property in

this case. The Department also indicated that it is in the process of updating its information guides to specifically identify those slats that do and do not qualify for the exemption. (T61).

Respondents argue Livingston lacks standing to file a claim for refund, because Jurgens, not Livingston, was the "person who made the overpayment." NEB. REV. STAT. 77-2708(2)(b). As the parties recognize in their briefing, the issue of standing turns on whether Jurgens acted as an "Option" 1 or "Option 2" contractor. As discussed further below, if Jurgens acted as an "Option 1" contractor then Jurgens was not the consumer of the hog slats but the retailer, and Livingston was the purchaser of the hog slats and the "person who made the overpayment." In that situation Livingston has standing. If Jurgens acted as an "Option 2" contractor, however, then Jurgens was the hog slats consumer, purchaser, and the taxpayer. In that situation Livingston lacks standing.

STANDING

A party must have standing before a court can exercise jurisdiction, and either a party or the court can raise a question of standing at any time during the proceeding. *Frenchman-Cambridge Irr. Dist. v. Dept. of Nat. Res.*, 281 Neb. 992, 801 N.W.2d 253 (2011). Standing involves a real interest in the cause of action, meaning some legal or equitable right, title, or interest in the subject matter of the controversy. *In re Interest of Enyce J. & Eternity M.*, 291 Neb. 965, 870 N.W.2d 413 (2015). Under NEB. REV. STAT. 77-2708(2)(b), only the person who made the overpayment has a real interest in the controversy of a sales tax refund claim. *Aline Bae Tanning, Inc. v. Neb. Dep't of Revenue*, 293 Neb. 623, 627, 880 N.W.2d 61, 65 (2016). In order to determine who has standing to file a claim for a sales tax refund, the court employs the legal incidence test and "look[s] backward from the point at which [the Department] receives the

revenue until [one] find[s] the person legally liable for payment under the statute." *Id.* at 630, 880 N.W.2d at 67; *Anthony, Inc. v. City of Omaha,* 283 Neb. at 877, 813 N.W.2d at 476 ("[t]he legal incidence test requires a determination of who the law declares has the ultimate burden of the tax.").

A. "Retailers" and "Contractors."

A retailer is responsible for collecting the sales tax from consumers on each sale the retailer makes. *George Rose & Sons Sodding & Grading Co. v. Neb. Dep't of Revenue*, 248 Neb. 92, 95, 532 N.W.2d 18, 22 (1995). The sales tax collected constitutes a debt owed by the retailer to the state. *Id.* The retailer is responsible for remitting the sales tax to the state. *Id.* A contractor, as opposed to a retailer, is defined as "any person who performs any repair services upon property annexed to, or who annexes building materials to, real estate, including leased property, and who, as a necessary and incidental part of performing such services, annexes building materials to the real estate being so repaired or annexed or arranges for such annexation." NEB. REV. STAT. § 77-2710.10 (2009). As applicable to the facts of this case, this section further provides the contractor:

> (1) Shall be permitted to make an election that he or she will be taxed as a retailer in which case he or she shall not be considered the final consumer of building materials annexed to real estate;
>
> (2) Shall be permitted to make an election that he or she will be taxed as the consumer of building materials annexed to real estate, will pay the sales tax or remit the use tax at the time of purchase, and will maintain a tax-paid inventory;

NEB. REV. STAT. § 77-2701.10(1) to (2) (Reissue 2009).

The option provided in § 77-2701.10(1), referred to as "Option 1," allows the contractor to elect to be treated as a retailer. 316 N.A.C. § 1.017.02H. "Option 1 contractors are retailers of those building materials that become annexed." 316 N.A.C. § 1.017.05A. "Option 1 contractors must collect sales tax from all of their customers ... on the total amount charged for building materials they annex to real estate ...." 316 N.A.C. § 1.017.05C(1).

The option provided in § 77-2701.10(2), referred to "Option 2," allows the contractor to elect to be treated as a consumer of building materials who pays sales tax at the time of purchase. 316 N.A.C. § 1.017.02I. "Option 2 contractors are consumers of those building materials that become annexed." 316 N.A.C. § 1.017.06A. "Option 2 contractors must pay the sales tax on all building materials and other taxable items when purchased or received." 316 N.A.C. § 1.017.06C(2).

The key determination before the court in resolving the question of whether Livingston has standing to file a sales tax refund is whether at the time of the hog slats transactions Jurgens was acting as an Option 1 contractor, in which case Livingston has standing, or an Option 2 contractor, in which case Livingston lacks standing.

Livingston argues Jurgens, not WPC, acted as a Option 1 contractor and retailer. Jurgens paid WPC for the hog slats in full, including $32,478.80 in sales tax. Livingston argues the record establishes that Jurgens was acting as its retailer. The court disagrees.

A contractor's election of how it will treat building materials for tax purposes is not made on a case-by-case basis. Rather, "[t]he choice of an option is made by the Nebraska Department of Labor's online Contractor/Subcontractor Registration Application located at

www.dol.nebraska.gov. The contractor/subcontractor registration information, including the contractor option elected, is displayed in the Contractor Registration Database." 316 N.A.C. § 1.017.03. "The option selected applies to all construction contracts." 316 N.A.C. § 1.017.03A. The court notes, however, there is no evidence in the record of the Jurgens' Contractor Registration Application or the status of Jurgens' official contractor option election. Nevertheless, the court can infer from the record that Jurgens has elected to operate as an Option 2 contractor.

The facts as they relate to standing are undisputed. In a letter to the Department, dated May 25, 2016, counsel for Livingston correctly summarized the relevant facts, which are: "[Jurgens], as the contractor on a building project for Livingston, purchased the concrete hog slats from [WCP]. The amounts paid by Jurgens to WCP for the concrete hog slats included the applicable amount of sales tax. Livingston then paid Jurgens for such amounts." (T66). These facts make clear Jurgens elected to be an Option 2 contractor. Even though Livingston paid for the hog slats and ultimately used the slats once they were installed, the only taxable event under these facts is the sale between WCP and Jurgens. By paying sales tax on the hog slats at the time of the purchase, Jurgens acted as an Option 2 contractor.

The facts show Jurgens was not acting as an Option 1 contractor or retailer. The only party to remit tax to the Department in this case was WCP. (T2). Jurgens did not remit the sales tax portion of Livingston's payment to the Department. Had Jurgens been a retailer it would have been obligated to do so. But Livingston's reimbursement to Jurgens was not a taxable sale. Jurgens merely passed on the cost of the sales tax to Livingston. As an Option 2 contractor,

Jurgens was the consumer, and not the retailer, of the hog slats. Jurgens was the purchaser and, therefore, the taxpayer.

Under the Department Regulations, even an Option 2 contractor can be considered a retailer if it sells building materials or other property that is not annexed. 316 N.A.C. § 1.017.06D(1). "Annexed means attached to real estate so that: (1) the property becomes real estate,; or (2) the installation or removal of the property requires specialized skills or tools and is performed or supervised by a recognized trade professional." 316 N.A.C. § 1.017.02A. The primary evidence in the record on this issue is an email exchange between the parties. (T57-63). Livingston, who bears the burden of proof, argues the hog slats are not annexed, because they are removable and anyone could remove them. (T2). Conversely, Respondents provide a more detailed description, stating the "concrete gang slats and other building materials become an integral part of the building once installed since they effectively become the floor of the building." *Id.* In support of this description, Respondents cite to *Iowa Ag Constr. Co.*, 723 N.W.2d 167. While acknowledging the decision in this Iowa case was based on a factual record that is not before the court, the court finds *Iowa Ag Constr. Co.* persuasive to the extent that Respondents have shown some legal support for their position. Furthermore, the court finds the installation of the hog slats required specialized skills or tools and was performed by Jurgens, a recognized trade professional. The court finds the hog slats were annexed to real property. "Property that becomes annexed to real estate loses its identity as tangible personal property." (T61, 63). Jurgens, an Option 2 contractor, was not acting as a retailer in this case.

WCP was a retailer of building materials. Jurgens was the purchaser and consumer of the hog slats. Jurgens was the taxpayer and had the ultimate burden of the tax. WCP remitted the

sales tax paid by Jurgens to the Department. Livingston reimbursed Jurgens for the sales tax, but Jurgens did not remit any payment made by Livingston to the Department. Livingston is not the party who made the tax overpayment under § 77-2708(2)(b). Livingston lacks standing to claim a sales tax refund. The court need not reach the merits of Livingston's claim for overpayment.

IT IS, THEREFORE, ORDERED, ADJUDGED AND DECREED that the Tax Commissioner's denial of Livingston's claim for overpayment is affirmed. Costs of this appeal are to be taxed to Petitioner Livingston.

DATED this 25 day of January, 2017.

BY THE COURT:

Jodi L. Nelson
District Court Judge

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