STATE OF ALABAMA DEPARTMENT OF REVENUE,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
v.	§	DOCKET NO. S. 85-160
S.E.A. WIRE & CABLE, INC. 110 Celtic Circle Madison, Alabama 35870,	§	
Taxpayer.	§	

ORDER

This case involves two disputed preliminary assessments entered by the Department against the Taxpayer concerning State sales tax for the period April 1, 1983 through December 31, 1984, and City of Madison sales tax for the period July 1, 1983 through December 31, 1984. A formal hearing was conducted by the Administrative Law Division on December 18, 1985. The parties were represented at said hearing by attorneys E. Dwight Fay, Jr., for the Taxpayer, and assistant counsel J. Wade Hope, for the Department. Based on the evidence submitted at the hearing, the following findings of fact and conclusions of law are hereby made and entered.

FINDINGS OF FACT

The relevant facts are undisputed. In December, 1983, the Taxpayer donated wire and cable to the Alabama Aviation and Technical College in Ozark, Alabama. The merchandise bad been purchased by the Taxpayer at wholesale at a cost of $15,231.57. The fair market value of the merchandise at the time of donation was $28,754.97, as indicated on the Taxpayer's federal income tax return. It is undisputed that the Alabama Aviation and Technical

College is an exempt educational institution within the purview of Code of Alabama 1975, §40-23-4(a)(15).

The Revenue Department audited the Taxpayer for the period in issue and set up the wire and cable donation as a taxable retail sale in the amount of $15,231.57. The Department's position is that the withdrawal of the materials, which had been previously purchased at wholesale, from inventory was for the personal and private use of the Taxpayer and thus was a taxable retail sale under Code of Alabama 1975, §40-23-1(a)(10).

The Taxpayer argues that because the Technical College is a tax exempt entity, neither a sale nor a gift to the college should be subject to sales tax. Also, the Taxpayer contends that the withdrawal was not a retail sale under §40-23-1(a)(10) because the material was not withdrawn for a personal and private use or consumption, and also, because there was a transfer of title to the property, contrary to the subsection (a)(10) definition of a retail sale.

CONCLUSIONS OF LAW

Prior to 1983, the "withdrawal for use" or "self-consuming" provision of §40-23-1(a)(10) read in pertinent part as follows:

> (10) SALE AT RETAIL or RETAIL SALE.... The term "sale at retail" or "retail sale"shall also mean and include the withdrawal, use or consumption of any tangible personal property by anyone who purchases same at wholesale . . . .

The purpose of the above provision was stated by the Court of Civil Appeals in

State v. Kershaw Manufacturing Company, Inc., 372 So.2d 1325 (1979)

as follows:

> The "self-consuming" features of the statutes were enacted to reach transactions which could not otherwise be taxed because, although there Is a withdrawal from inventory by the purchaser at wholesale, there is no subsequent sale by him to another. State v. Barnes, 45 Ala. App. 522 , 233 So.2d 83 (1970). In order for tax liability to obtain ln a particular "self consuming transaction " there must, of necessity, be a personal and private use or consumption by the manufacturer. See e.g., State v. Kershaw Mfg. Co., 273 Ala. 215, 134 So.2d 740 (1962).

The Provision has been cited as authority to tax a variety of transactions, including the withdrawal of raw materials by a manufacturer for use in fulfilling a personal obligation under a construction contract, Alabama Precast Products, Inc. v. Boswell, 357 So.2d 985 (1978),

and the withdrawal of carpet by & wholesale purchaser to fulfill its obligations under a furnish

and install contract, Home Tile and Equipment Company v. State, 352 So.2d 236 (1978),

among others.

In 1983, the legislature amended the withdrawal provision of §40-23-1(a)(10) to read as follows, with relevant changes under-lined:

> (10) SALE AT RETAIL or RETAIL SALE..... The term "sale at retail" or "retail sale" shall also mean and include the withdrawal, use or consumption of any tangible personal property previously purchased at wholesale, by a person engaged in the business of selling at retail tangible personal property from the business or stock for the personal and private use or consumption, without transfer of title, in connection with the business or by the person so withdrawing, using or consuming the same, except property which has been previously withdrawn from the business or stock and so used or consumed and with respect to which property tax has been paid because of such previous withdrawal, use or consumption, and except

> property which enters into and becomes an ingredient or component part of tangible personal property or products manufactured, fabricated or compounded for sale or for use in the performance of a contract for improvements or additions to real estate situated outside the state of Alabama; and such wholesale purchaser shall report and pay the taxes thereon. (emphasis added)

The appellate courts in Alabama have issued four opinions concerning the withdrawal provision subsequent to passage of the 1983 amendment. Set out below is a brief discussion of those four cases.

The first case to be decided was Ex parte Disco Aluminum Products Co., Inc. v. State, 455 So.2d 849 (1984). In that case, the taxpayer purchased raw materials at wholesale and thereafter withdrew and used said materials to fabricate windows and doors which it subsequently installed outside of Alabama pursuant to a furnish and install contract. The period in issue was prior to the effective date of the 1983 amendment. The Revenue Department argued that the pre-amendment statute should apply, and cited pre-amendment case law in support of its decision to tax the withdrawals. The Supreme Court recognized that prior case law supported the Department, but nonetheless ruled against the Department, holding that the 1983 amendment was merely declaratory of existing law and therefore should be applied retroactively. By application of the 1983 amendment, the transactions were clearly not taxable under the last portion of the amended section underlined above in that the transactions involved withdrawals of

property "for use in the performance of a contract for improvements or additions to real estate situated outside the state of Alabama".

The next case to be decided was White v. Campbell and Associates, Inc., 473 So.2d 1071, which was decided by the Court of Civil Appeals on May 1, 1985, with certiorari denied by the Supreme Court on August 23, 1985. In the Campbell case, the issue was whether the withdrawal from inventory of rubberlining materials that had been previously purchased at wholesale, and used to rubberline pipes, etc. belonging to others and which were subsequently returned to the owners for use or sale, was a taxable withdrawal under §40-23-1(a)(10). The Court held that the withdrawal and use constituted a retail sale as follows:

> . . . However, such acceptance does not prevent the conclusion that the withdrawal and consumption of the manufactured rubber lining in the performance of a personal contract (the lining, of another's property) comes within the definition of a "retail sale" as provided by §40-23-1(a)(10). Unlike the situation in Ex parte Disco Aluminum Products Co., 455 So.2d 849 (Ala. 1984), the title to the materials consumed is not transferred or sold. What Campbell sells to its customers that give it objects to rubberline is not a "manufactured" rubber lining. It sells its capability to produce and apply the rubber lining.
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> [4] The purpose of §40-23-1(a)(10) is to reach and tax transactions which do not fall within the usual definition of a retail sale. Otherwise there would be no taxable event. Alabama Precast Products, Inc. v. Boswell, 357 So.26 985 (Ala.1978). The situation at hand fits squarely within the criteria for a taxable withdrawal under §40-23-1(a)(10).

The Court of Civil Appeals again addressed the withdrawal provision in Morrison Food Service of Alabama, Inc. v. State of

Alabama, (hereinafter, Morrison (1)), Civ. 4775 (July 24, 1985). The Department entered assessments against Morrison based on the withdrawal by Morrison of food from its inventory for use in the completion of food service contracts. Morrison was obligated to furnish food for various hospitals, nursing homes and fraternities, and also to provide supervisory personnel to manage the programs. The Court recognized that because of the 1983 amendment changes, and the resulting decision, that preamendment case law was not controlling. Rather, the Court relied on its recent decision in White v. Campbell and Associates, Inc., supra. The two cases were compared as follows:

> Instead, we turn to a case decided recently by this court and subsequent to the passage of the amendment to section 40-23-1(a)(10) In this case, White, Commissioner v. Campbell & Associates, Inc. [Ms. May 1, 1985] (Ala. Civ. App. 1995), the State sought to impose a sales tax under the withdrawal provision, § 40-23-1(a)(10), Code 1975 (Supp. 1984), on materials used by Campbell in its rubberlining process. The State imposed the tax on rubber lining materials that Campbell withdrew from inventory to rubber line pipes that belonged to others. The State did not attempt to tax withdrawals of rubber lining materials which were used to rubber line pipes manufactured by Campbell and then sold. We stated that "the title to the materials consumed is not transferred or sold. What Campbell sells to its customers that give it objects to rubberline is not a 'manufactured' rubber lining. It sells its capability to produce and apply the rubber lining." Likewise, Morrison sells to its customers its ability to purchase large volumes of food at a discount and its expertise in preparing tasteful meals for large groups of people. Title to Morrison's raw materials is not transferred or sold; rather it is compounded under Morrison's supervision into meals

> and then served to 'its customer's patients or members.
>
> Morrison cannot argue that title was transferred or sold after its raw materials were compounded into meals and then served to its customer's patients. In ARA Hospital Food Management, Inc. v. State, supra, we stated "[the hospitals purchased no tangible personal property; they purchased a service. As the trial court correctly found: "Here, the contractor has undertaken the [hospital's] responsibility to provide patient food service and stands in the shoes of the [hospitals] . . . as the consumer of the food and not as a seller of meals."

The most recent decision concerning the withdrawal provision is Ex parte: State of Alabama, Department of Revenue, Re: State v. Morrison Cafeterias Cons. Inc. (hereinafter Morrison (2)), 19 AER 3413 (Aug. 30, 1985). In that case, the issue was whether food withdrawn from inventory by Morrison and given to Morrison employees as partial wage payments was a taxable withdrawal under §40-23-1(a)(10). The Supreme Court held for the Department, citing the 1961 case State v. T. R. Miller Mill Company, 130 So.2d 185, which held that a retail sale occurred when a lumber manufacturer withdrew logs and other raw materials previously purchased at wholesale to make necessary repairs and improvements to its facility. The Court stated as follows:

> We cannot distinguish T. R. Miller Mill Co. from the present case. Morrison purchases raw food at wholesale. This food is prepared and sold at retail, at which time a sales tax is paid. Morrison withdraws some portion of this food from its inventory, however, and that portion is used for Morrison's own purposes, is not sold, and therefore escapes taxation. The intention of the

> legislature was to close this tax loophole with the "self-consuming" provision.

Turning to the case at hand, the determinative issue concerns the effect of the phrase set out below, which was added to the withdrawal provision by the 1983 amendment.

> The terms "sale at retail" or "retail sale" shall also mean and include the withdrawal, use or consumption . . . <u>for the personal and private use or consumption, without transfer of title</u>, in connection with the business or by the person so withdrawing, using or consuming the same . . . . (emphasis added)

None of the four post-amendment cases discussed above provide a direct discussion as to the meaning and effect of the above language. Because of the added language, a valid argument could be made that the provision is now limited to only those situations where the wholesale purchaser withdraws property and thereafter personally consumes it, such as a grocer taking food from the grocery store shelf for personal consumption. Only in such instances would there be no eventual transfer of title to the property. Such an interpretation would sharply reduce the scope of the withdrawal provision, and, contrary to the original intent of the legislature, would result in no tax being paid on transactions in which property Is purchased at wholesale and withdrawn for use in satisfying a contract or obligation of the withdrawer, with title to the property being transferred to another party. The eventual transfer of title would remove the transaction from the subsection (a)(10) definition of retail sale.

However, from a reading of the Morrison (1), Morrison (2), and Campbell cases, it appears that the appellate courts do not accept that such a literal interpretation should be applied to the amendment changes. In Campbell, ownership (title) to the rubberlining materials that were withdrawn and used by the taxpayer was eventually transferred to the owners of the objects that had been rubberlined by the taxpayer. However, the Court found that for purposes of the withdrawal provision, "the title to the materials consumed is not transferred or sold". In Morrison (1), the taxpayer withdrew food and transferred it to its customer's patients for consumption. Again, the Court held that for purposes of determining the applicability of §40-23-2(a)(10), "title to Morrison's raw materials is not transferred or sold". Finally, in Morrison (2), the Court did not directly discuss the transfer of title to the food in question, but did find that the withdrawal and transfer of the food by Morrison to fulfill its obligations to its employees was a taxable withdrawal.

> Morrison withdraws some portion of this food from its inventory, however, and that portion is used for Morrison's own purposes, is not sold, and therefore escapes taxation. The intention of the legislature was to close this tax loophole with the "self-consuming" provision.

It is clear from the above cases that if property previously purchased at wholesale is withdrawn and used to fulfill an obligation of the withdrawer, then the appellate courts still consider such a transaction to be a taxable withdrawal for use,

notwithstanding that ownership or title to the withdrawn property may be eventually transferred to another party. The taxable event is the withdrawal and use or consumption by the taxpayer, and any subsequent transfer of title beyond that taxable event is inconsequential for purposes of applying the withdrawal provision. Such an interpretation preserves the original intention of the legislature to tax property that is purchased at wholesale and not resold, but rather, is used by the wholesale purchaser.

However, the instant case presents a factual situation that has not yet been addressed in Alabama. Unlike the typical withdrawal provision cases discussed above, in which the subject property is withdrawn and subsequently used by the withdrawing party to fulfill a contract or obligation, in the case in issue the Taxpayer withdrew the wire and cable and, without obligation, donated it to the Technical College. That is, there was no intervening personal and private use by the Taxpayer between the withdrawal of the materials and the subsequent transfer of title to the Technical College. The donation satisfied no legal obligation of the Taxpayer. Accordingly, because title to the wire and cable was transferred, with no "personal and private use or consumption" by the Taxpayer, the withdrawal and donation of the wire and cable by the Taxpayer was not a taxable event under §40-23-1(a)(10), as amended.

It is, recognized that the above holding results in the subject

property escaping taxation, a result that the withdrawal provision was originally intended to prevent. However, the intent of the Legislature can only be determined from the plain language of the statute, Brundidge Milling Co. v. State, 288 So.2d 475 (1969); Boswell v. South Central Bell Telephone, 301 So.2d 65 (1974), and the amended withdrawal statute provisions that there must be a personal and private use, without (prior to) transfer of title. From a review of the cases discussed above, it is clear that the appellate courts have continued to apply the withdrawal provision to situations where the withdrawing party uses the property to fulfill an obligation or contract, unless the use concerns an improvement to property outside of the State, as in Disco. The withdrawal and use is the taxable event, and any subsequent transfer of title is of no consequence. However, if there is no personal and private use or consumption by the withdrawer prior to transfer of title, then under the plain wording of the statute, as amended, the transaction is not taxable. In the present case, there was no such use or consumption. Thus, there was no retail sale under subsection (a) (10) .

Notwithstanding the finding for the Taxpayer, for the record it should be noted that the basis used by the Department in calculating the proposed liability, i.e. the Taxpayer's wholesale cost of the materials, was improper. Under §40-23-1(a)(6), the taxable measure of property that is withdrawn for use is "the

reasonable and fair market value" of the property at the time of withdrawal. In the present case, the fair market value of the materials when donated was $28,754.97, as indicated by the Taxpayer's income tax return. Thus, if the transaction had been subject to the withdrawal provision, the proper taxable measure would have been $28,754.97, not $15,231.57.

Based on the above, it is hereby determined that the assessments in issue should be reduced to zero and thereafter made final by the Department.

Done this 27th day of January, 1986.

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BILL THOMPSON
Chief Administrative Law Judge