IN THE SUPREME COURT OF MISSISSIPPI

JOSEPH BLOUNT, in his official capacity as chairman and commissioner of the Mississippi State Tax Commission — **APPELLANT**

VS. — **NO.: 2006-CC-00673**

ECO RESOURCES, INC. — **APPELLEE**

Appeal from the Chancery Court of Harrison County, Mississippi Second Judicial District

---

BRIEF OF APPELLEE

LUTHER T. MUNFORD (MSB#[redacted]
C. DELBERT HOSEMANN, JR. (MSB#[redacted]
R. GREGG MAYER (MSB#[redacted])
PHELPS DUNBAR LLP
111 E. Capitol Street, Ste. 600
Jackson, MS 39201
Telephone: (601) 352-2300
Facsimile: (601) 360-9777

ATTORNEYS FOR APPELLEE

ORAL ARGUMENT REQUESTED

IN THE SUPREME COURT OF MISSISSIPPI

JOSEPH BLOUNT, in his official capacity as chairman and commissioner of the Mississippi State Tax Commission — **APPELLANT**

VS. — **NO.: 2006-CC-00673**

ECO RESOURCES, INC. — **APPELLEE**

CERTIFICATE OF INTERESTED PARTIES

The undersigned counsel of record certifies that the following listed persons have an interest in the outcome of this case. These representations are made so that the judges of this Court may evaluate possible disqualification or recusal.

1. ECO Resources, Inc., plaintiff and appellee

2. Luther Munford, C. Delbert Hosemann, Jr., and Gregg Mayer, Phelps Dunbar LLP, Jackson, Mississippi, counsel for ECO Resources, Inc.

3. Mississippi cities who hire professional water system managers.

4. Mississippi State Tax Commission

5. Dave Scott, attorney for the Mississippi State Tax Commission.

LUTHER T. MUNFORD
Counsel of record for ECO Resources, Inc.

STATEMENT REGARDING ORAL ARGUMENT

The issues here are legal questions that should not require oral argument, but oral argument is requested so that ECO Resources, Inc. can respond to any new contentions the State Tax Commission may make in its reply brief.

Miss. Code Ann. § 27-65-21, which lists the "activities" subject to the contractor's tax, includes the repair of a "sewer . . . or water system." It then provides: "Such activities shall not include . . . repairing or adding to . . . property which retains its identity as personal property."

The question is whether the statutory personal property repair language limits the taxation of repairs to sewer or water systems. The plain language, the legislative history, and the State Tax Commission's prior practice, all lead to the conclusion that the tax does not apply to the repair of property that is part of a sewer or water system but retains its identity as personal property.

The Chancellor also did not manifestly err by relying on and applying the personal property definition found in the Commission's memorandum on this issue, which the Tax Commission Brief endorses but does not quote.

For these reasons, this Court should affirm the judgment entered by that court.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

FEDERAL CASES

STATE CASES

STATE STATUTES

MISCELLANEOUS

STATEMENT OF THE ISSUES

The Chancellor held that buried pipes used in sewer and water systems are real property, but that pumps and other machinery retain their identity as personal property because they can be removed without altering or destroying the structure to which they are attached.

1. When Miss. Code Ann. § 27-65-21 imposes a tax on "activities which include the repair of "sewer, irrigation water systems," are those activities limited by subsequent language which says "[s]uch activities" shall not include the repair of "any property which returns its identity as personal property"?

2. If so, did the Chancellor manifestly err by defining "personal property" as a 1999 Tax Commission memorandum defined it when that definition is consistent with Mississippi law, is similar to definitions used in other states, and is endorsed by the Tax Commission in its brief, an endorsement inconsistent with the position the brief otherwise advances?

These are questions of first impression which are of importance to every local government in Mississippi which hires a professional service company to manage its water or sewer system.

INTRODUCTION

ECO Resources Inc. provides professional services to cities. 2:10 Specifically, it manages water and sewer systems. In so far as this case is concerned, it does *not* build systems. It does *not* add to systems. Ex. 16 §§ 1.04, 1.05, RE 54-55. All it does is keep them going in compliance with state and federal regulations.

It monitors pumps to ensure that they are working, checks water to ensure it is sufficiently pure, bills and collects from customers, provides security, cleans buildings, provides insurance, and, on occasion, marks the location of lines for others so the other person's digging will not damage the lines. Ex. 16, RE 53-80; 2:15, 22-28.

Occasionally, it repairs pumps, fixes meters, and performs other similar services. 1:114, RE 7; 2:22-28. In the chancery court it proved *both* that i) these services were a tiny percentage – about 8% of its activities – and that, in any event, ii) any repairs were to personal property.[1] See p. 6, *infra*. The State Tax Commission offered no proof on the personal property issue. It instead maintained that the contractor's tax applies to repairs to both real and personal property that is

[1] The Tax Commission's claim that taxpayer ECO did not prove that the 59% figure was "in any way unreasonable, arbitrary, capricious, or not supported by substantial evidence" is just wrong. See Tax Commission Brief at 14. ECO did not place "all of its eggs in one basket." It put them in two baskets. The Chancellor selected one of ECO's baskets and so had no reason to rule on the other. See 1:62-66, 69-77, 81-84 (ECO post-trial findings and conclusions). That is why, even if the Chancellor's order were reversed, the relief would be a remand, not a remedy in favor of the Commission.

part of a water system because the phrase "water system" appears in the statute. See 3:232 (Commission witness says above-ground transmission line would be personal property but work on it would be taxed). Alternatively, it argued that no personal property is used in a "water system."

The Chancellor correctly rejected the Tax Commission's tortured reading of the statute. In so doing, he properly relied on the statutory language, and the memoranda and regulations of the State Tax Commission, all of which recognize that repair of personal property – defined as property that can be removed without alteration or destruction of a structure – is not subject to the contractor's tax.

This Court should affirm the Chancellor's decision, which, as the legislature no doubt intended, reduces the cost of these services to the local governments who run water and sewer systems and to the taxpayers who support them.

STATEMENT OF THE CASE

Proceedings below. The Brief of Appellant ("Tax Commission Brief") adequately states the course of proceedings below at pp. 2-3.

Statement of facts. Although this case concerns ECO contracts with five Mississippi cities over a three-year period, the parties stipulated that its contract with Biloxi in 1999 was a representative contract and most of the testimony centers on that contract. 1:114-115, RE 7-8.

The contract is a contract for "Professional Services." Ex. 16, RE 53-80. It expressly states that it does not include either the construction of water or sewer

lines nor does it include the extension of any lines. *Id.* at §§ 1:04, 1:05. *See also* 1:16; Ex. 14, RE 49-50. It simply involves billing and the maintenance of the system and, if necessary, repairs where the labor cost is below $2,000. The contract expressly prohibits it from performing repairs that cost more than $2,000. *Id.* at § 1.03; 2:18-19.[2]

For the year of 1999, ECO paid $22,232 in sales taxes to the state for its Biloxi work. This included taxes on materials purchased as well as taxes on certain work performed for third parties and taxes on some construction work that was outside the original contract. It did not pay taxes on the labor part of the professional services contract. Ex. 1, RE 81-103.

In 2000, state tax commission auditor Dorothy Cooper demanded that the company pay an additional $25,495 in sales taxes for its 1999 Biloxi work pursuant to the contractor's tax statute, Miss. Code Ann. § 27-65-21 (2005). *See* Appendix. Ex. 1, RE 81-103. She based this on a calculation that 70% of the company's work involved repairs to property. She arrived at that figure simply by looking at job titles of its employees in Biloxi. 2:141; 3:179-182. She conceded

[2] Miss. Code Ann. § 27-65-105(a) (2005) exempts from taxation "[s]ales of labor . . . taxable under . . . § 27-65-23 in when sold to" a municipality. For that reason, ECO did not engage in "any business in which a tax is levied in Section 27-65-23," and so owes no tax under that statute, which governs miscellaneous businesses such as plumbing, either directly under § 23 or indirectly through § 21. In any event, the Tax Commission has not chose to defend the tax here on that basis. 3:229-230.

that 30% of the company's work, such as collecting bills from customers, could not be taxed.

In calculating what company "activities" were taxable, she took "crew member" to mean "construction crew member" even though the contract excluded construction work. 3:184. She classified 100% of the time of the contract manager's and safety coordinator's time as being contractor work. She did this because, she said, they were important to performing the contract. 3:155. *See also* 2:113; 3:202-205. She considered marking water lines for others so they could avoid cutting a line to be taxed because it is "all a part of that one contract." 3:189-190, 215 ("everything to be one maintenance contract."); *see* 3:269-71. She included inspections because they might have led to a repair. Ex. 1, RE 81-103. Finally, she made no allowance for services provided to residential property, which the statute expressly excludes from taxation. 3:211-212.

ECO Resources paid the additional taxes, appealed, and argued that no more than 10% of its services were subject to tax, if any tax were due. Ex. 40, RE 18-27. After a Board of Review accepted Moore's conclusions, the State Tax Commission cut her percentage down to 59%. Ex. 11, RE 43-44. It did so because it recognized the need to exclude residential services from the work taxed. 3:249-265; Ex. 22, RE 32-33; Ex. 24, RE 35-42; RE 25. As to the personal property limitation, it simply declared that the statute taxes work on "water systems." Ex. 11, RE 43-44.

At trial, ECO proved that Moore's use of job categories, which the Commission had adopted, was irrational. Activities such as marking lines for third parties had nothing to do with repair, and neither did sampling water or monitoring sewer pumps. "Crew members" did not construct anything because the contract forbids it, Ex. 16 at §§ 1.04, 1.05, RE 53-80, as would state purchasing law.

ECO's expert testified that, at best, only 8% of ECO's activities could be said to be in the nature of a repair. 1:118, RE 11; 2:96-111; Ex. 34, 35 (inspections, meter reading, customer service, preventative maintenance are "non-taxable" services).

ECO also proved that the pumps, meters, chlorination devices, and so forth it repaired could be removed without damage to real property, were intended to be replaced, and were of use only in connection with the water and sewer systems. See *infra* pp. 16-17. The chancellor later physically examined a water well site and a sewage lift station to ensure that this was true. 1:121, RE 14. The State Tax Commission offered no contrary proof.

The Chancellor found that the pumps and meters were personal property under the definition found in a Tax Commission memorandum, Ex. 38, RE 104-05, and so held that work on them was not subject to the contractor's tax. 1:121-122, RE 14-15. *See* Appendix. He held that the water and sewer lines themselves were real property, their removal would damage the real estate, but found that none of

ECO's services reflected in Ex. 34 or other evidence could reasonably be interpreted as work on the "underground" pipes. 1:122, RE 15.

Accordingly, the Chancellor ruled that the Tax Commissioner should refund the additional taxes ECO had paid, with interest.

SUMMARY OF ARGUMENT

The legislature has said that charges for activities such as repairs to water or sewer systems may be taxed, but "such activities" do not include repairs to property "which retains its identity as personal property." Miss. Code Ann. § 27-65-21(1)(a)(i) (2005).

The Tax Commission makes two equally unsustainable attempts to argue that all repairs to any of the property of a water system may be taxed.

First, it wrongly argues that the phrase "sewer . . . or water system" means the whole system, without distinguishing between the system's real property and its personal property. But that interpretation conflicts with the distinction the statute itself makes, is contrary to the legislative history, and is even contrary to the Tax Commission's prior interpretation of the statute.

Then the Tax Commission wrongly argues that, in any event, a "water system" is entirely real property and none of it is personal property. But that is obviously not what the legislature thought when it amended the statute to distinguish between real and personal property. Nor is the argument consistent with the Tax Commission's interpretative memorandum, which the Tax

Commission endorses in its brief. Ex. 38, RE 104-05 (*See* Appendix). That memorandum says property is personal property if it can be removed without altering or destroying the structure to which it is affixed. The Chancellor did not manifestly err by applying the Tax Commission memorandum's test to the facts in evidence here and concluding that the property ECO repairs is personal property.

ARGUMENT

I. The repair of personal property that is part of a water system is not subject to the contractor's tax.

Interpretation of statutes presents a question of law, which this court reviews de novo. As this Court has held, it will not enforce a ruling of the State Tax Commission that is "repugnant to the plain meaning of a statute." *Oxy USA, Inc. v. Mississippi State Tax Commission*, 757 So.2d 271, 274 (Miss. 2000); *Mississippi State Tax Commission v. Lady Forest Farms, Inc.*, 701 So.2d 294, 296 (Miss. 1997). This is particularly true where the Commission's interpretation is fraught with inconsistencies. *Id.* The duty to defer to an agency interpretation "has no material force where the agency interpretation is contrary to the statutory . . . language." *Mississippi State Tax Commission v. Moselle Fuel Co.*, 568 So.2d 720, 723 (Miss. 1990).

Moreover, as this Court has said in interpreting the same statute, "It is familiar learning that doubts in tax statutes should be resolved in favor of the taxpayer." *Stone v. W.G. Nelson Exploration Co.*, 51 So.2d 279, 282 (Miss. 1951).

In this case, the text, the legislative history, and the memoranda and rules of the State Tax Commission all lead to only one conclusion: repairs to property that is part of a water system and maintains its identity as personal property are not subject to the contractor's tax.

A. The text says personal property repairs that are part of "such activities," including water and sewer system repairs, are not taxed.

In material part, § 27-65-21 (2005) provides:

> (1)(a)(i). Upon every person engaging or continuing in this state in the business of contracting or performing a contract or *engaging in any of the activities, or similar activities, listed below* for a price ...there is hereby levied ... a tax equal to three and one-half percent (31/2% of the total contract price or compensation received ... from constructing, building, erecting, *repairing* ... any building, highway...culvert, *sewer*, *irrigation or water system* ... railway, reservoir, dam, power plant, ... water well, any other improvement or structure or any part thereof .... *Such activities shall not include constructing, repairing or adding to property which retains its identity as personal property....*
>
> (b) The following shall be excluded from the tax levied by this section:
>
> (i) The contract price or compensation received for ... repairing ...any other improvement or structure which is *used for or primarily in connection with a residence or dwelling place for human beings.*

Id. (emphasis added). *See* Appendix.

The statutory language could hardly be plainer. The word "activities" provides the key. The statute refers to "activities . . . listed below." Sewer and

water systems are among the listed "activities." Then the statute says "such activities" shall not include repairing "property which retains its identity as personal property."

To be sure, the Commission can tax the repair of water systems, but not to the extent that repair involves the repair of personal property that is a part of such a system.

The Code defines "repair" as "the restoring of property in some measure to its original condition, which may involve the use of either personal property or labor or both . . . ." Miss. Code Ann. § 27-65-11 (2005).[3]

B. The legislative history shows that personal property repairs were eliminated from all activities taxed by the statute as part of an attempt to lower taxes on contractors.

From 1934 to 1982, the Contractor's Tax statute did not make any reference to personal property repairs. In that year, however, the legislature added to the section, almost at its end, the sentence stating that the tax did not apply to repairs of personal property. 1982 Miss. Laws. Ch. 442 § 1. At the same time, it added the residential properties exception, § 2, and abolished the former statewide privilege tax on those who bid on or perform construction contracts, § 3.

[3] The statutory word is "repair," not "maintenance," and, in any event "maintenance" has the same definition as repair. Miss. Code Ann. § 27-65-11. It does *not* mean "the upkeep of property or equipment," which is what maintenance can mean in other contexts. See Webster's NEW COLLEGIATE DICTIONARY 693 (1977). There is no merit to the Tax Commission's attempt to expand the meaning of "repair" by using the phrase "maintenance and repair."

The legislature's placement of the personal property sentence, as well as its language, indicates that personal property repairs are not to be taxed. That the sentence was coupled with the abolition of a privilege tax on contracts demonstrates a legislative intent to cut the tax burden on contractors generally. That purpose is wholly consistent with the way the Chancellor read the statute, and is wholly inconsistent with the way the State Tax Commission reads it.

Furthermore, courts have debated for years what portions of a utility's property should be considered real property for taxation purposes. Generally, a contractor's tax like the one in issue here applies only to repairs to real property. That is because "a real property contractor is considered the ultimate consumer of property for purposes of imposing the sales tax." 85 C.J.S. *Taxation* § 2031 ("Contractors; Public Contracts"). *See e.g. Rudolph v. Potomac Elec. Power Co.*, 24 F.2d 882, 883 (D.C. Ct. App. 1928) (lines located over streets belonging to the U.S. were personal property).

C. The Tax Commission has historically read the statute not to include repairs to personal property.

The chancellor relied in part on a State Tax Commission memo which not only recognizes the personal property limitation on the scope of the contractor's tax, but also defines what the Commission considers to be "personal property." Ex. 38, RE 104-05 (*See* Appendix). *See* 1:116, 121-122, RE 9, 14-15; 2:86-87.

That memo recognizes that water and sewage systems are subject to the contractor's tax, but then goes on to describe the personal property limitation without any indication that it does not apply to personal property used by water or sewer systems. The Commission's present claim that the personal property limitation does not apply to personal property used by water or sewer systems is inconsistent with that memorandum.

D. Rules of construction cannot change the text, the legislative purpose, and the past administrative interpretation of the statute.

Where the meaning of a statute is plain, there is no room for principles of statutory construction. *Oxy USA, Inc. v. Mississippi State Tax Commissio*n, 757 So.2d 271, 274 (Miss. 2000). In *Oxy USA, Inc.*, this Court set aside a Commission ruling that had imposed a tax on gas injected back into oil wells because it contradicted the plain language of the relevant statute, it was inconsistent with other law, and the Commission had taken different positions on the question over time.

The Commission's arguments against the plain language of the statue need not be considered but, if considered, should be rejected. Their weakness begins with the Commission's contention that plain language governs while it brief makes no attempt to explain the critical personal property language in the statute. The silence is telling. Brief of Appellant 14-15.

Nor does the exemption for repairing entire utility systems in emergencies help the Commission's case. *Id.* at 16 *citing* Miss. Code Ann. § 27-65-21 (1)(b)(iii) (exemption for price to repair "utility or distribution system" if repair "performed by the entity providing the service at its cost"). It is perfectly consistent to say that, generally, repairs of personal property are not taxed and, in an emergency, repairs to *both* personal and real property, i.e., the entire "utility system," are not taxed.

The only purpose of maxims of construction is to determine the legislative intent. The intent here is clear and, in any event, the maxims do not help the Commission. The distinction between repair of personal and real property is part of the paragraph that defines the tax. It does not supply an exclusion from activities otherwise taxed. So cases concerning exemptions are not even relevant. Moreover, it is not clear which is more specific: repair of buildings or repair of personal property. So the specific versus general argument cannot carry the weight the Commission puts on it in this case. See Tax Commission Brief at 19.

As a result, the mass of citations in the Tax Commission Brief at 14 to 19 count for nothing. None of them interprets the language in issue here. All of them simply state general rules of construction which either do not apply here or, if they apply, support ECO's interpretation of the statute. The legislature "[broke] apart the water and sewer systems" into components, i.e., real and personal property.

Tax Commission Brief at 11. That is not just an ECO "suggestion." *Id.* It is the law.

II. The chancellor did not err in applying the Commission's definition of personal property.

A. In an appeal from the Tax Commission, the chancellor conducts a trial de novo and this Court owes deference to his findings.

The appeal of a Tax Commission ruling "does not contemplate mere appeal on the record as by certiorari but inescapably implies an original action in which the entire merits of the case may be heard that the liability of the taxpayer adjudged ...." *Stone v. Kerr*, 10 So.2d 845, 848 (Miss. 1942). That, this Court said, was essential to providing an adequate remedy at law that would make injunctive relief against the Tax Commissioner unavailable. To that end, the legislature has provided for a trial *de novo* in the chancery court to determine tax liability.

First, the statute for hearings before the Commission says "Any appeal to chancery court . . . shall include a full evidentiary judicial hearing on the issues presented." Miss. Code Ann. § 27-77-5(6) (2005). Then the appeal statute says the chancellor is to "try the case de novo and conduct a full evidentiary judicial hearing on the issues raised." It provides:

> At trial of any action brought under this section, the chancery court shall give deference to the decision and interpretation of law and regulations by the commission as it does with the decisions and interpretation of any administrative agency, but it shall try the case de novo and conduct a full evidentiary judicial hearing on the issues raised. Based on the

> evidence presented at the hearing, the chancery court shall determine whether the taxpayer has proven, by a preponderance of the evidence ...that he is entitled to any or all of the relief he has requested.

Miss. Code Ann. § 27-77-7 (2005).

Because the trial is de novo, the chancellor has the power to make findings of fact to which this court will defer unless manifest error is shown. *Mississippi State Tax Commission v. ANR Pipeline Co.*, 806 So.2d 1081, 1084 (Miss. 2002) (where appeal statute requires trial de novo in chancery court, review is to determine whether chancellor's findings were "manifestly wrong, clearly erroneous, or contrary to the weight of the evidence."); 84 C.J.S. *Taxation* § 773 (where tax appeal tried de novo appellate court "will not interfere with a finding based on conflicting evidence").

B. The chancellor's findings that the equipment on which ECO works is moveable and removable without altering or destroying the structures in which it is placed is not manifestly erroneous, and the Tax Commission does not challenge that factual finding.

As this case comes to this Court, it is to be taken as a given that the equipment on which ECO works is moveable and can be removed without altering or destroying the structures in which it is placed.

In the chancery court, ECO filed pre-trial findings which made it clear that it contended that the property repaired was personal, and not real property. At trial it elicited testimony from the Commission auditor, Ms. Moore, that she did not take that distinction into account when she did her audit. 3:164-165, 172-173, 193, 267.

She believed repairs to anything located on commercial property were subject to the tax. 3:170. Similarly, the Tax Commission made no findings on the personal property question to which a court would owe deference. 3:233 (review board did not discuss distinction).

ECO introduced into evidence photographs of a pump and an electrical box typical of the type found in the Biloxi system. Its witnesses testified that they have the characteristics of personal property, e.g., they can be removed without altering or destroying real property. 2:67-75, 92-93; Exs. 32A, 32B. See also p. 17, *infra*. That is the key difference between personal and real property the Commission has followed in the past. Ex. 38, RE 104-05 (*See* Appendix).

Here, the Chancellor said the equipment on which ECO worked was not permanently attached:

> The Court finds that the services taxed by STC as being subject to the contractor's tax were performed on personal property. The evidence, including the testimony of ECO's expert witness, Ralph Ellison, describing the components and makeup of typical water and sewer systems, as well as the Court's inspection of a sewer lift station and a water well site (both a part of the Biloxi system (Exhibit 16)) establish that the components on which ECO performed its services retained their identity as personalty.

The court continued:

> The components consist generally of pumps, electrical motors, floats, control panels, chlorination devices. None of these devices are permanently attached to real property. In fact, they are easily removed for repair or

> replacement without causing any alteration or damage to the structure on which they are mounted. Once removed, they can be used at different locations

RE 1:121-122, RE 14-15. The evidence, testimony, personal inspection by the Chancellor, and exhibits offered at trial, fully supports the chancellor's findings that the equipment could be removed "without causing any alteration or damage to the structure on which they are mounted." 2:67-75, 92-93, 120-122; Exs. 32A, 32B, 41A, 41B. *See* 2:91 ("the pipes in the ground, . . . things just don't happen to them").

These findings are correct, and have certainly not been shown to be manifestly erroneous. In fact, the Commission's Brief does not even appear to challenge them.

C. The chancellor did not manifestly err by adopting the Tax Commission's traditional definition of personal property.

The Commission's argument concerning the definition of personal property is, like Tax Commission positions in the past, "fraught with inconsistency." *Mississippi State Tax Commission v. Lady Forest Farms, Inc.*, 701 So.2d 294, 296 (Miss. 1997).

On the one hand, the Tax Commission says that the destruction or alteration of structures test found in its memo on the question is correct. The Commission's Brief at 26 says that its 1999 internal memo on the Contractor's Tax, Ex. 38, RE 104-05 (*See* Appendix), "condensed and summarized the relevant portions of Rule

41." That rule, in turn, admits that "[c]ontracts for the performance of work on personal property . . . are not subject to the [contractor's tax]."[4] The Tax Commission Brief also says that its memorandum states the correct rule of Mississippi law. See Tax Commission Brief at 25 (the "personal property exemptions for component materials [in Rule 41] . . . is nothing other tha[n] an expression of settled common law in Mississippi regarding the realty/personal property analysis").

The memo, which the Commission's brief does not quote, defines the difference between real and personal property for purposes of the contractor's tax. Where, as here, the property is not an independent structure, the test is alteration or destruction of the structure to which it is attached:

> For personal property to be considered real property, it must be permanently attached to real property. To be considered permanently attached, one or more of the following criteria must be met:
>
> * The property or equipment must be attached to building walls, floors and/or ceiling in such way as to require design or structural alterations to the real property to which it is being attached, or
>
> * The property could not be removed intact or its removal would result in the alteration or destruction of the structure or real property...

[4] Codified as Mississippi State Tax Commission Regulation IV-10-01-306, Tax Commission Brief Appendix.

Ex. 38.[5] This Tax Commission definition is not the only possible definition of personal property. Definitions vary according to the area of law involved. But the objective standard it embodies is easy to enforce and is consistent with the holdings of numerous Mississippi cases. See *Motorola Communications and Electronics, Inc. v. Dale*, 665 F.2d 771, 773 (5th Cir. 1982) (Miss. law) (radio transmission tower could be removed without material injury); *Weathersby v. Sleeper*, 42 Miss. 732, 1869 WL 2726 at *6 (Miss. Err. & App. 1869) (saw mill could be removed without injury to property, and so was personalty).[6]

Motorola, which termed *Weathersby* "perhaps the leading case" in Mississippi on the distinction between real and personal property, quoted it not only for a "serious injury" test, but also for the proposition that if the classification is "a matter left in doubt or uncertainty, the legal qualities of the article are not changed and it must be deemed a chattel." 665 F.2d at 773.

The same or a similar distinction has been made in other states. *See e.g. Ladish Malting Co. v. Stutsman County*, 351 N.W.2d 712, 714 (N.D. 1984) (state constitution says machinery is personal property for tax purposes unless it supports building or would cause damage when removed; cites a "material injury" test used

[5] It goes on to refer to "built-in furniture, fixtures, appliances, and similar personal property." Ex. 38, RE 104-05 (*See* Appendix).

[6] *Bondafoam, Inc. v. Cook Const. Co., Inc.*, 529 So.2d 655, 658 (Miss. 1988) (bridge timbers could be removed); *Fidelity-Phenix Fire Ins. Co. v. Redmond*, 144 Miss. 749, 111 So. 366, 368 (1926) (fixtures could not be removed without damage so were realty); *Boone v. Mendenhall Lumber Co.*, 97 Miss. 554, 52 So. 584 (1910) (engine bolted to foundation was personalty)

for taxation in New Jersey and a "movability" test used in New York); *Johnston v. United States*, 1979 WL 1537 at *5 (D. Mont. 1979) (under federal tax regulation, sewage treatment plant in mobile home park, including pumps and lifts, was personal property except for pipes which could not be moved without digging up land).[7]

If this test applies, then the chancellor correctly analyzed the case.

Perhaps for that reason, the Commission then turns around and makes an entirely different argument about the definition of personal property. Rather than stick to its alteration or destruction test, it urges the use of a four part intent test and argues that, under that test, there is no personal property at all in a "water system." Tax Commission Brief at 21. It says the Court should not "isolate and focus upon component parts of either system." *Id.*

Certainly, where the Tax Commission takes two inconsistent positions, the chancellor did not err in choosing only one of them, i.e., by using the "alteration or destruction" test and finding that ECO repaired personal property, not underground pipelines.

[7] *Nickerson Pump and Machinery Co. v. State Tax Commission*, 361 P.2d 520, 522 (Utah 1961) (water pumps were personal property after installation because they were readily removable without harm to structures); 71 Am Jur. 2d *State and Local Taxation* § 143 (tax law definition of "not to be severed without material injury" was same as common law).

In any event, the legislature did not consider the whole water system to be real property, because that would render the repair to personal property language in the statute meaningless. The Commission's argument proves too much.[8]

Moreover, some of the cases the Commission cites from other jurisdictions recognize that machines connected to pipes can be personal property, *General Motors Corp. v. City of Linden*, 696 A.2d 683, 687 (N.J. 1997); *Zangerle v. Standard Oil Co. of Ohio*, 60 N.E.2d 52, 58 (Ohio 1945), *limited by Litton Systems, Inc. v. Tracy*, 728 N.E.2d 389, 391 (Ohio 2000) (equipment was personal property; *Zangerle* "too eagerly applied fixture analysis").

In the final analysis, the Commission's attempt to switch definitional horses is not just an indicator that its present statutory construction is unsound. Rather, it is itself an arbitrary and capricious action. Taxpayers should be able to rely on the law the Tax Commission says it is following, and not be subject to paying taxes, penalties, and interest 11 years after 1996 because the Tax Commission has now changed its mind – maybe.

Moreover, there is a legislative definition of personal property. It includes "goods, chattels, effects..." Miss. Code Ann. § 1-3-41 (2005). If the Tax

---

[8] One case the Tax Commission cites reaches the same result the Chancellor reached, i.e., that pipelines are real property. See *Paris Mountain Water Co. v. Woodside*, 131 S.E. 37, 40 (S.C. 1925). A trial court decision the Tax Commission cites holds that a light pole is real property, but does not consider other aspects of the system. *Cleveland Electric Illumination Co. v. Continental Express*, 733 N.E.2d 328 (Ohio Ct. Com. Pl. 1999). *In re Lido Beach Sewage Collection Dist.*, 243 N.Y.S.2d 223 (NY. Co. Ct. 1963) does not consider whether some part of a sewage system might be personal property.

Commission wants a more detailed definition, all it has to do is ask the legislature for it.

CONCLUSION

The ultimate question here is how much ratepayers who use a Mississippi water or sewer system will have to pay for those services. Increasing the taxes on a professional services contractor, as the Commission seeks to do here, will only increase the prices those contractors will have to charge those who hire them, who are usually governmental units of one sort or another. *See* Miss. Code Ann. § 27-65-31 (Rev. 2005). It will benefit the state at the expense of the local governmental units.

Quite logically, the legislature eliminated repairs to personal property from the activities taxed in order to reduce the local burden. The statutory language is clear. The Chancellor's findings concerning the classification of property follow the written position the Tax Commission has taken and are fully supported by the evidence.

For these reasons, this Court should affirm the chancellor's ruling or, in the alternative only, remand to the chancellor for consideration of the remaining issues in the case.

RESPECTFULLY SUBMITTED, this the 25th day of January, 2007.

ECO RESOURCES, INC.

BY: _____

LUTHER T. MUNFORD (MSB[redacted]
C. DELBERT HOSEMANN, JR.
(MSB#[redacted]
R. GREGG MAYER (MSB#[redacted])
PHELPS DUNBAR LLP
111 E. Capitol Street, Ste. 600
Jackson, MS 39201
Telephone: (601) 352-2300
Facsimile: (601) 360-9777

COUNSEL FOR APPELLEE

CERTIFICATE OF SERVICE

I do hereby certify that I have this date mailed through the United States Postal Service, postage prepaid, a true and correct copy of the above and foregoing BRIEF OF APPELLEE to the following:

Mr. Dave Scott
Post Office Box 1033
Jackson, MS 39215-1033

Mr. Michael Cavanaugh
998 Howard Avenue
Biloxi, MS 39530

Chancellor Jim Persons
Post Office Box 457
Gulfport, MS 39502

This the 25 day of January, 2007.

LUTHER T. MUNFORD

APPENDIX

and lands, there is hereby levied, assessed and shall be collected a tax equal to one and one-half percent (1½%) of the gross proceeds of such retail sales of the business.

SOURCES: Laws, 1990 Ex Sess, ch. 71, § 21, eff from and after passage (approved June 30, 1990).

Editor's Note — Laws, 1990 Ex Sess, ch. 71, § 25, effective June 30, 1990, provides as follows:

"SECTION 25. Nothing in Sections 21 through 23 of this act shall affect or defeat any claim, assessment, appeal, suit, right or cause of action for taxes due or accrued under the Mississippi Sales and Use Tax Laws prior to the effective date of this act, whether such assessments, appeals, suits, claims or actions shall have been begun before such date or shall thereafter be begun; and the provisions of the aforesaid statutes and amendments thereto are expressly continued in full force, effect and operation for the purpose of the assessment, collection and enrollment of liens for any taxes due or accrued and executing of any warrant thereunder prior to the effective date of this act, or the filing of reports, and for the imposition of any penalties, forfeitures or claims for failure to comply therewith."

§ 27-65-21. Contracting, etc.

(1)(a)(i) Upon every person engaging or continuing in this state in the business of contracting or performing a contract or engaging in any of the activities, or similar activities, listed below for a price, commission, fee or wage, there is hereby levied, assessed and shall be collected a tax equal to three and one-half percent (3½%) of the total contract price or compensation received, including all charges related to the contract such as finance charges and late charges, from constructing, building, erecting, repairing, grading, excavating, drilling, exploring, testing or adding to any building, highway, street, sidewalk, bridge, culvert, sewer, irrigation or water system, drainage or dredging system, levee or levee system or any part thereof, railway, reservoir, dam, power plant, electrical system, air conditioning system, heating system, transmission line, pipeline, tower, dock, storage tank, wharf, excavation, grading, water well, any other improvement or structure or any part thereof when the compensation received exceeds Ten Thousand Dollars ($10,000.00). Such activities shall not include constructing, repairing or adding to property which retains its identity as personal property. The tax imposed in this section is levied upon the prime contractor and shall be paid by him.

(ii) Amounts included in the contract price or compensation received representing the sale of manufacturing or processing machinery for a manufacturer or custom processor shall be taxed at the rate of one and one-half percent (1½%) in lieu of the three and one-half percent (3½%).

(b) The following shall be excluded from the tax levied by this section:

(i) The contract price or compensation received for constructing, building, erecting, repairing or adding to any building, electrical system, air conditioning system, heating system or any other improvement or structure which is used for or primarily in connection with a residence or

dwelling place for human beings. Such residences shall include homes, apartment buildings, condominiums, mobile homes, summer cottages, fishing and hunting camp buildings and similar buildings, but shall not include hotels, motels, hospitals, nursing or retirement homes, tourist cottages or other commercial establishments.

(ii) The portion of the total contract price attributable to design or engineering services if the total contract price for the project exceeds the sum of One Hundred Million Dollars ($100,000,000.00).

(iii) The contract price or compensation received to restore, repair or replace a utility distribution or transmission system that has been damaged due to ice storm, hurricane, flood, tornado, wind, earthquake or other natural disaster if such restoration, repair or replacement is performed by the entity providing the service at its cost.

(c) Sales of materials and services for use in the activities hereby excluded from taxes imposed by this section, except services used in activities excluded pursuant to paragraph (b)(iii) of this subsection, shall be subject to taxes imposed by other sections in this chapter.

(2) Upon every person engaging or continuing in this state in the business of contracting or performing a contract of redrilling, or working over, or of drilling an oil well or a gas well, regardless of whether such well is productive or nonproductive, for any valuable consideration, there is hereby levied, assessed and shall be collected a tax equal to three and one-half percent (3½%) of the total contract price or compensation received when such compensation exceeds Ten Thousand Dollars ($10,000.00).

The words, terms and phrases as used in this subsection shall have the meaning ascribed to them as follows:

"Operator" — One who holds all or a fraction of the working or operating rights in an oil or gas lease, and is obligated for the costs of production either as a fee owner or under a lease or any other form of contract creating working or operating rights.

"Bottom-hole contribution" — Money or property given to an operator for his use in the drilling of a well on property in which the payor has no interest. The contribution is payable whether the well is productive or nonproductive.

"Dry-hole contribution" — Money or property given to an operator for his use in the drilling of a well on property in which the payor has no interest. Such contribution is payable only in the event the well is found to be nonproductive.

"Turnkey drilling contract" — A contract for the drilling of a well which requires the driller to drill a well and, if commercial production is obtained, to equip the well to such stage that the lessee or operator may turn a valve and the oil will flow into a tank.

"Total contract price or compensation received" — As related to oil and gas well contractors, shall include amounts received as compensation for all costs of performing a turnkey drilling contract; amounts received or to be received under assignment as dry-hole money or bottom-hole money; and shall mean and include anything of value received by the contractor as remuneration for

services taxable hereunder. When the kind and amount of compensation received by the contractor is contingent upon production, the taxable amount shall be the total compensation receivable in the event the well is a dry hole. The taxable amount in the event of production when the contractor receives a production interest of an undetermined value in lieu of a fixed compensation shall be an amount equal to the compensation to the contractor if the well had been a dry hole.

(3) When the work to be performed under any contract is sublet by the prime contractor to different persons, or in separate contracts to the same persons, each such subcontractor performing any part of said work shall be liable for the amount of the tax which accrues on account of the work performed by such person when the tax heretofore imposed has not been paid upon the whole contract by the prime contractor.

When a person engaged in any business on which a tax is levied in Section 27-65-23, also qualifies as a contractor, and contracts with the owner of any project to perform any services in excess of Ten Thousand Dollars ($10,000.00) herein taxed, such person shall pay the tax imposed by this section in lieu of the tax imposed by Section 27-65-23.

Any person entering into any contract over Seventy-five Thousand Dollars ($75,000.00) as defined in this section shall, before beginning the performance of such contract or contracts, either pay the contractors' tax in advance, together with any use taxes due under Section 27-67-5, or execute and file with the Chairman of the State Tax Commission a good and valid bond in a surety company authorized to do business in this state, or with sufficient sureties to be approved by the commissioner conditioned that all taxes which may accrue to the State of Mississippi under this chapter, or under Section 27-67-5 and Section 27-7-5, will be paid when due. Such bonds shall be either (a) "job bonds" which guarantee payment when due of the aforesaid taxes resulting from performance of a specified job or activity regardless of date of completion; or (b) "blanket bonds" which guarantee payment when due of the aforesaid taxes resulting from performance of all jobs or activities taxable under this section begun during the period specified therein, regardless of date of completion. The payments of the taxes due or the execution and filing of a surety bond shall be a condition precedent to the commencing work on any contract taxed hereunder. Provided, that when any bond is filed in lieu of the prepayment of the tax under this section, that the tax shall be payable monthly on the amount received during the previous month, and any use taxes due shall be payable on or before the twentieth day of the month following the month in which the property is brought into Mississippi.

Any person failing either to execute any bond herein provided, or to pay the taxes in advance, before beginning the performance of any contract shall be denied the right to perform such contract until he complies with such requirements, and the commissioner is hereby authorized to proceed either under Section 27-65-59, under Section 27-65-61 or by injunction to prevent any activity in the performance of such contract until either a satisfactory bond is executed and filed, or all taxes are paid in advance, and a temporary injunction

enjoining the execution of such contract shall be granted without notice by any judge or chancellor now authorized by law to grant injunctions.

Any person liable for a tax under this section may apply for and obtain a material purchase certificate from the commissioner which may entitle the holder to purchase materials and services that are to become a component part of the structure to be erected or repaired with no tax due. Provided, that the contractor applying for the contractor's material purchase certificate shall furnish the State Tax Commission a list of all work sublet to others, indicating the amount of work to be performed, and the names and addresses of each subcontractor.

SOURCES: Codes, 1942, § 10110; Laws, 1934, ch. 119; Laws, 1936, ch. 158; Laws, 1942, ch. 122; Laws, 1944, ch. 129, § 3; Laws, 1950, ch. 530, § 2; Laws, 1955, Ex sess, ch. 109, § 11; Laws, 1956, ch. 420, § 1; Laws, 1958, ch. 574, § 8; Laws, 1962, ch. 598, §§ 1, 3; Laws, 1964, ch. 532, § 2; Laws, 1968, ch. 588, § 5; Laws, 1982, ch. 442, § 1; Laws, 1984, ch. 458, § 1; Laws, 1985, ch. 351, § 3; Laws, 1987, ch. 432; Laws, 1996, ch. 503, § 2; Laws, 1997, ch. 320, § 1; Laws, 2005, ch. 434, § 1, eff from and after July 1, 2005.

Editor's Note — Laws, 1992, ch. 421, § 1, provides as follows:

"SECTION 1. No municipal or county official shall issue a building permit to any person unless the person provides information satisfactory to the issuing official that the person complies with Section 27-65-21, Mississippi Code of 1972, or provides information satisfactory to the issuing official that the requirements of Section 27-65-21, Mississippi Code of 1972, do not apply to the person."

Amendment Notes — The 2005 amendment inserted "under Section 27-65-61" following "Section 27-65-59" in the next-to-last paragraph of (3).

Cross References — Applicability of tax levied by this section to solid or hazardous waste treatment projects, see § 17-17-131.

Income tax, see §§ 27-7-1 et seq.

Application of the term "wholesale sales" to § 27-65-21, see § 27-65-5.

Taxation of certain component materials of contracts taxable under this section, see § 27-65-15.

Sales tax revenues collected under this section being excepted from monthly allocation to municipalities, see § 27-65-75(1).

Exclusion of tax revenue collected under this section in making monthly allocation and distribution of sales tax revenues to municipalities, see § 27-65-75.

Industrial exemptions from sales tax, see § 27-65-101.

Agricultural exemptions from sales tax, see § 27-65-103.

Governmental exemptions from sales tax, see § 27-65-105.

Utility exemptions from sales tax, see § 27-65-107.

Tax related exemptions from sales tax, see § 27-65-109.

Other exemptions from sales tax, see § 27-65-111.

Applicability of tax to agriculture and industry program, see § 57-3-33.

Applicability of this tax to mortgages, leases and purchases required to establish an industrial enterprise and financed by proceeds from bonds issued pursuant to chapter 10, title 57, Mississippi code of 1972, see § 57-10-255.

Contractors' tax imposed by this section as exception to tax exempt status of bonds issued to finance economic development projects, see § 57-10-439.

Certain purchases made pursuant to Small Enterprise Development Finance Act not exempt from contractor's tax imposed under this section, see § 57-71-13.

Distribution of proceeds derived from contractor taxes levied under this section on contracts for construction or reconstruction of highways designated under § 65-3-97, see § 27-65-75.

(38)

For your Information

MISSISSIPPI STATE TAX COMMISSION
SALES & USE TAX BUREAU

Memo

To: Kathy Waterberry
From: Carl Carlisle
Date: January 20, 1999
Re: Contractors

Please inform the Districts of the following changes effecting contractors.

1) **Continuous contracts** on a project embracing activities taxable under Section 27-65-21 for a definite period of time and a definite amount will be qualified and taxed at 31/2%. Otherwise, the determination of a taxable contract will be from purchase orders, work orders or invoices. Purchase orders, work orders or invoices that are a continuation of prior purchase orders, work orders or invoices will be considered one project.

2) **Rebuild utility distribution or transmission system** -- As of March 27, 1997, contractor's tax will not apply to the contract price or compensation received to restore, repair, or replace a utility distribution or transmission system (electric, gas, water, sewage, telephone, etc.) damaged by an ice storm, hurricane, flood, tornado, wind, earthquake or other natural disaster if the entity performing the restoration, repair or replacement is reimbursed for its cost only.

3) **Component materials** are considered all materials that become an integral part of the structure being erected. For personal property to be considered real property, it must be permanently attached to real property. To be considered permanently attached, one or more of the following criteria must be met:

   - The property or equipment must be attached to building walls, floors, and/or ceiling in such way as to require design or structural alterations to the real property to which it is being attached, or
   - The property could not be removed intact or its removal would result in the alteration or destruction of the structure or property, or
   - The property must become an independent structure, itself real property
   - And the property must lose its identity as personal property.
   - Component materials include built-in furniture, fixtures, appliances and similar personal property

4) Liquidating damages that are withheld by the owner are not to be included in taxable contract receipts

5) Casinos -- Effective July 1, 1996, a 31/2% tax will be levied on the gross proceeds or gross receipts from the sale of any tangible personal property that becomes a component part of the structure or

Exhibit 38 Case #_____
Evd ✓ ID_____ Date_____

the performance of any construction activity upon any floating structure. These floating structures are normally moored and not normally engaged in the business of transporting people or property. These structures are located within the waters of the State of Mississippi. This tax does not apply to tangible personal property that does not become a component part of the structure. If one contractor is doing both the land based and floating structure construction, this tax may be paid by the contractor, otherwise, the owner of floating structure is responsible for the tax. The owner of a floating structure, subject to the 31/2% tax, will be issued a distinctive number similar to an MPC Number. The owner will provide this number to the prime contractors and sub-contractors. This will allow the purchase of component materials and parts for use in the construction activities exempt from further sales tax.

The owner of a floating structure will also be issued a direct pay number. (Refer to Rule #8 for Direct Pay Number treatment) With the use of the MPC number and this direct pay number, tax is accrued on the owner's use tax return and not paid to vendors

6) **Assisted Living** – Any complex being constructed that provides any type of assisted living, is to be qualified, if over $10,000. It does not matter if the assisted living is provided by medical or non-medical personnel.