Wyoming Law Journal

Volume 8 | Number 2 Article 3

December 2019

Transfer of Possession as a Taxable Sale

Thomas J. Fagan

victed murderer, who was still living, was barred from inheriting through him. The murderer was convicted of the felonious killing of his mother. The son of the murderer, i.e., the grandson of the deceased, brought an action claiming the estate of the deceased, basing his contention on the fact that his father was precluded by statute from inheriting, and that he was the rightful heir. The Court said, "Other lineal descendants are so appointed only in case there is no child of the intestate living at the time of her death. Despite the serious charge against him, decedent's son was living at the time of decendent's death, hence other lineal descendants are not appointed by law to succeed to her real estate."[23] The Court ruled that the grandson was disqualified from inheriting, and permitted the sister of the deceased to take instead.

Those statutes with a provision for the conviction of a murderer are not without pitfalls.[24] For example, a Kansas case[25] held that a verdict by the coroner's jury that the deceased had been killed by her husband, was not a conviction within the contemplation of the Kansas statute. Since the killer had committed suicide before the trial, there could be no conviction. Consequently, the wife's property was inherited by the husband, and, at his death, went to his heirs.

The interpretation of the statutes by our three sister states would indicate a negative answer to our topic question, i.e., does the Wyoming statute require a conviction. None of the states in making their rulings in the probate court, have held themselves bound by the fact that there was a conviction of the murderer, and all seem to follow the construction that without express legislation on how to proceed in the matter, they will decide the cases on the merits.

LEONARD E. LANG

TRANSFER OF POSSESSION AS A TAXABLE SALE

A large number of states have enacted legislation assessing a tax upon retail sales. Most, if not all, of the laws governing such tax have incorporated in them a definition of the term sale. This article is concerned with those laws that define the term sale, as does Wyoming's,[1] as including a "transfer of possession of tangible personal property for a consideration." The courts have recognized that this is an extremely broad definition of the term and have by court decision, qualified it to a greater or lesser degree. The purpose of this paper is to point out some of the more common "tests" the courts have applied in determining if a transfer of possession is such as to constitute a taxable retail sale.

23. Id. at 380, 162 P.2d 379.
24. Wade, supra note 3, at 723.
25. Hogg v. Whitham, 120 Kan. 341, 242 Pac. 1021 (1926).

1. Wyo. Comp Stat. 1945, Sec. 32-2502.

In determining if a transfer of possession is a taxable sale the courts have often considered if the transfer arrangement is one that takes the place of a sale; i.e. even though the transaction is accompanied by legal mechanics other than a sale, such as a lease, it in effect accomplishes the same purpose. A California Intermediate Court[2] placed great emphasis upon the term "in lieu of sales" in determining if a transfer of possession was a taxable sale. The statute of California,[3] under which this case was decided, qualified its definition of sale so as to include only transactions that were "in lieu of transfer of title". This case involved a transfer of drilling equipment (bits) to a drilling contractor under a lease arrangement; the manufacturor of the drilling equipment being the "lessor". Even though there was no tranfer of title involved and the "lessee" was ultimately to return the bits to the "lessor", the court held the transaction was taxable as a sale, inasmuch as the equipment was "substantially consumed" under one lease agreement. There is an indication that the courts would so hold even in the absence of such a qualifying statement in the statute. An Iowa case[4] involved a transfer of possession of personal property in which the transferor entered into a written contract, with the parties specifically stating the contract was one for services. The court in holding the transaction constituted a taxable sale said: "The fact that he (transferor) does enter into a written contract does not of itself make the transaction a contract for service rather than for . . . sale of personal property. He (transferor) can call this what he pleases. The question is what is it under the statute."[5] The Code of Iowa,[6] under which the case was decided, defines sale as "any transfer, exchange or barter . . . in any means . . . for a consideration." An Arkansas decision,[7] while not specifically referring to the phrase "in lieu of transfer of title," applied a test which in effect amounted to the same thing. The court said, in holding a transfer of possession was not a taxable sale, "The transfer of possession . . . means a transfer that in effect amounts to a sale. The legislature intended to tax sales under whatever disguises they might masquerade."[8] In refusing to accept, without qualification, the statutory definition of sale[9] as a mere transfer of possession, the court said: "Wherever it can be said there is a sale on a lease or rental basis, it must have some of the charcteristics of a sale, and not be a lease or a rental in fact."[10] A study of the cases in point show a trend of the courts to look beyond the technical legal arrangements in determining if a transfer of possession, with no transfer of title, constitutes a taxable sale. In looking beyond the legal arrangements the courts will consider if

2. Universal Eng. Co. v. State Board of Equalization, 256 P.2d 1059 (1953).
3. Deerings Calif. Codes, Revenue and Taxation, Sec. 6006, (a) (1943).
4. Kistner v. Iowa State Board of Assessment and Review, 225 Iowa 404, 280 N.W. 587 (1938).
5. Ibid.
6. Code of Iowa, 1935, Sec. 6943-f38(b).
7. U-Drive-Em Service Co. v. State by Hardin, Commissioner of Revenues, 205 Ark. 501, 169 S.W.2d 584 (1943).
8. Ibid.
9. The Arkansas Gross Receipts Act, 1941, Sec. 1, Act 386.
10. Supra note 7.

the transaction is in lieu of transfer of title or a sale in disguise. The effect of such reasoning is to defeat, in some instances at least, attempts to escape sales tax liability on transactions that are as a rule considered as sales. Such decisions also tend to "soften" the harshness of a literal interpretation of very broad definitions in statutes governing tax on retail sales.

Another test the courts have applied in determining the tax aspects of a transaction could be referred to as the "time test"; i.e. for what length of time does the transferee of an article have it in his possession? A recent Colorado case[11] involved a transfer of automobiles to customers by a concern engaged in the driverless car business. In this case the purchaser of the cars (the owner of the business) maintained that his customers and not he should be required to pay the sales tax as it was the customers who were the ultimate consumers of the cars. The Supreme Court of Colorado refused to sustain this contention and in holding that the customers were not subject to a sales tax on the transfers said: "We are of the opinion that the continuous possession contemplated by . . . the statute is not shown in this case." The Colorado court said, by way of dictum, "The type of transaction the law is intended to reach is the case of the caluclating machine . . . installed at lessees business and supervised by lessor under a rental agreement covering a continuous (and usually very considerable length of time) this involves a more permanent type of lease that the multifarious types, renting driverless cars for their various purposes." An Arkansas case[12] decided under a statute[13] that defined sale as "the transfer of . . . possession for a valuable consideration, of tangible personal property regardless of the manner . . . by which the transfer is accomplished" held that a transfer for a limited time did not constitute a taxable sale. The court said the character of the possession referred to in the Act is "the permanent possession . . . and not the temporary possession such as we have here." Although the cases cited above seem to indicate that the courts will consider the time element involved in determining if the transfer of possession is a taxable sale, there are decisions that overlook this element entirely. The New York Supreme Court[14] held that the transfer of motion picture films from a distributor to an exhibitor with license to use them for a specified length of time constituted a taxable sale. It is interesting to note that the case was decided under a law[15] very similar to Wyoming's in relation to its definition of sale. It has been held that the supplying of linen goods, i.e. towels, sheets, pillow cases, etc. to a hotel on a rental or service basis constitutes a taxable sale.[16] The court said in reference to time: "Possession was transferred and the transferee asserted possessory interest in the linen for such length of time as was necessary to carry out the purpose intend-

11. Herbertson v. Cruse, 115 Colo. 274, 170 P.2d 531, 172 A.L.R. 1312 (1946).
12. Supra note 7.
13. Supra note 9.
14. United Artists Corporation v. Taylor, 273 N.Y. 334, 7 N.E.2d 254 (1937).
15. Local Law No. 20, New York City (1934).
16. Philadelphia Assn. of Linen Suppliers et. al. v. City of Philadedphia, et al., 139 Pa. Super 560, 12 A.2d 789 (1940).

ed."[17] Certainly in neither of the last two cases was there ever any understanding on the part of either the transferor or the transferee that the latter was to buy the property involved. Bearing in mind the fact that all sales tax law is based upon statutes that have as their primary purpose the obtaining of revenue and which contain very broad definitions of the term sale it is not difficult to understand why many transactions will be taxed even though the parties to the transaction had no intention to enter into a buy and sell agreement. Many state's laws have included in their definitions of sale phrases that eliminate, to a great extent, the application of the "time test." The statute[18] involved in the Pennsylvania case cited[19] is typical of such statutes. In addition to the common broad definition, "any transfer of possession" it also states "or . . . license to use or consume conditionally or otherwise."

An important factor that the courts have taken into consideration in determining if a transfer of possession constitutes a taxable sale is whether the article transferred represents a service rather than a sale. An Illinois decision[20] held that the sale of blue prints, photostats and commercial photography were not retail sales within the provisions of the Retailer Occupation Tax Act.[21] The court in this case said: "We can perceive no logical difference between the paper upon which the photostatic copy of something is made . . . and that paper which a lawyer uses for drawing a will or a deed . . . the paper is a mere incident: the skilled service is that which is required." The Supreme Court of North Dakota[22] held contra in a case with very similar facts. In holding that the sale of photographs made to order for his customers was a taxable sale as opposed to a rendition of services, the court said: "there is no atricle fabricated by machine or fashioned by human hand that is not the fruit of the exercise and application of individual ability and skill . . . the product resulting is tangible personal property . . . it remains the property of the maker until it is paid for and delivered." The court decided the North Dakota case under a statute[23] very similar to that involved in the contra Illinois case.[24] Some cases[25] have held that a transaction may be in part only subject to a sales tax. These cases hold that when "an article sold has a definite value apart from the value, of the services rendered, . . . the value of the article may be separated from the value of the servcies and a tax may be levied on the sale, even though the contract may provide for one lump sum including both the rendition of services and the sale of goods."[26] The problem con-

17. Ibid.
18. Philadelphia City Sales Tax Ordinance, Sec. 1 (d) (1938).
19. Supra note 16.
20. J. A. Burgess Co. v. Ames, 359 Ill. 427, 194 N.E. 565 (1945).
21. Illinois Revised Statutes 1951, Vol. 2, C. 120, Sec. 440.
22. Voss v. Grey, 70 N.D. 727, 298 N.W. 1 (1941).
23. North Dakota Sales Tax Act.
24. Supra note 20.
25. Ahern v. Nudelman, 374 Ill. 237, 29 N.E.2d 268 (1940); Kistner v. Iowa State Board of Assessment and Review, 225 Iowa 404, 280 N.W. 587 (1938); Commonwealth v. Miller, 337 Pa. 246, 11 A.2d 141 (1940).
26. 139 A.L.R. 382.

cerning a rendition of service rather than a sale is often covered by statute. In holding that druggists receipts from sale of prescriptions were subject to the sales tax, the Supreme Court of Florida[27] upheld a statute that defined gross receipts as "total amount of sale price of retail sale, including any services which were a part of those sales."[28] The cases which consider the rendition of services as a factor in determining whether a transfer of possession is a taxable sale seem to follow generally three views. 1. That a transfer involving essentially a rendition of services is not a taxable sale. 2. That even though an article's value consists primarily of the vendor's service or skill the transfer is subject to a sales tax. (This is the minority view in the absence of statute covering such transactions) 3. The courts will take into consideration the part of the value of the article that is made up of services as opposed to the part of the value of the article in terms of physical worth and impose a sales tax on only the latter.

Many sales tax statutes or ordinances define a sale at retail as a transfer of title to tangible personal property for consumption or use and not for resale.[29] Cases arising in these jurisdictions force the courts to consider as a test in determining if a transfer of possession is a taxable sale whether or not the transferee intended to use or consume the article transferred. In applying this test, the problem becomes one of definition; i.e. what amounts to "use" or "consumption"? The courts have not hesitated to construe the terms "use" and "consumption" and typical of such definitions are: "We believe that the ordinary interpretation of the word 'use' is to assert possessory interest in the article for some length of time,"[30] is to assert the statute . . . 'use' means a long continued possession and employment of a thing for the purpose which it was adopted for as distinguished from a possession and employment there is merely temporary or occasional"[31]; "consume or consumption does not always imply an immediate destruction or eating up' or extermination; it may as well, and often does, contemplate the ultimate use to which all intermediate ones lead."[32] The California Intermediate Court[33] used language that is typical of the cases that define such terms as "use" and "consumption". The court said: "The word (s) 'consumed' as used in statutory provisions . . . are not technical words having a peculiar meaning in law, but are words in common use and must be given their plain ordinary meaning." The test of consumption or use is not necessarily confined to cases that have such a requirement set out in the statute and the test is often applied in conjunction with other tests including the ones referred to above.

The problem of determining what transactions constitute a taxable sale is one that must be approached almost entirely on a local basis. The

27. Wray's Pharmacy, Inc. et al. v. Lee, Comptroller, 145 Fla. 435, 199 So. 767 (1941).
28. Acts, 1935, C 16484, Sec. 2 (Florida).
29. 47 Am. Jur. 229.
30. Howitt v. Smith and S. Publications, 276 N.Y. 345, 12 N.E.2d 435 (1938).
31. Revzan v. Nudelman, 370 Ill. 180, 18 N.E.2d 219 (1938).
32. Albuquerque Lumber Co. v. Bureau of Revenue, 42 N.M. 58, 75 P.2d 334 (1937).
33. Supra note 2.

statutes governing such sales are far from uniform, in fact they . . . "exhibit a surprisingly large range of variation with respect to the precise activity or transaction taxed; the difficulties in attempting to reduce the term 'sales tax' to any single, all inclusive formula appear to be insurmountable."[34] Adding to the difficulty of formulating any guiding rules govering sales tax is the fact that all sales tax law is statutory and as such is subject to the whim of the legislators and are constantly being repealed and amended. In many cses, whether or not a transfer is subject to sales tax will depend upon the definition of terms in the statute. Most of the statutes have incorporated in them their own definitions of the terms, and here again they are far from uniform. The one thing such definitions seem to have in common is the fact that they are far broader than the usual laymen's concept of the term, and under the majority of the statutes the mere fact a transaction does not have all the usual characteristics of a sale does not necessarily mean it will not be taxable as such.

The case law on this subject is comparatively new (about 20 years) and as time goes on it is possible the decisions of the courts on the subject will become more uniform. The "tests" pointed out in this paper are certainly not meant to be a conclusive solution as to what transfers of possession are suche as to constitute a taxable sale, but they do indicate an approach the courts have, to some extent at least, adopted.

THOMAS J. FAGAN

THE MEASURE OF DAMAGES FOR BREACH OF AN EXPRESS COVENANT TO DRILL A TEST WELL

When a Wyoming mineral owner or the owner of an oil and gas lease desires to have a test well drilled on his land or lease he may lease or assign, as the case may be, all or part of his interest in return for a covenant to drill a well. Probably the most common arrangement of this type is the "farmout" in which one party assigns a block of acreage to another party in return for a promise to drill a well. If the assignor retains an undivided interest in the lease he is in effect exchanging a percentage of the lease for a test well and whatever income he will derive from his retained interest, which ordinarily will be a carried working interest, net profit interest, oil payment, or overriding royalty. On the other hand if the assignor assigns all of his interest in a particular block of acreage he probably expects to profit from the enhanced value, resulting from the drilling, of any surrounding acreage he might own. It is at once apparent that there are various opportunities for profit in these situations and consequently when the obligor breaches his covenant to drill it is only natural that the courts, in an attempt to do full justice to both parties, should adopt several rem-

34. 47 Am. Jur. 194.