STATE OF ALABAMA DEPARTMENT OF REVENUE,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
v.	§	DOCKET NO. S. 93-367
CENTRAL ALABAMA HOME EQUIPMENT CO., INC. 1517 West Street Montgomery, Alabama 36106, Taxpayer.	§	

OPINION AND PRELIMINARY ORDER

The Revenue Department assessed State lease tax and also State, Autauga County, Butler County, Crenshaw County, Lowndes County and local city sales tax against Central Alabama Home Equipment Company ("Taxpayer") for the period July 1988 through August 1992. The Taxpayer appealed the final assessments to the Administrative Law Division.

The Taxpayer subsequently moved to have the final assessments dismissed on procedural grounds. The Taxpayer's motion was denied by Orders dated April 12, 1994 and May 6, 1994. A hearing on the merits was conducted on June 8, 1994. Richard A. Lawrence represented the Taxpayer. Assistant counsel Wade Hope represented the Department.

The Taxpayer is in the business of leasing and selling durable medical equipment in Montgomery and the surrounding counties. Most of the Taxpayer's customers are covered by Medicare B Insurance.

The issues in dispute are as follows:

(1) Are gross receipts received by the Taxpayer from Medicare subject to Alabama sales or lease tax;

(2) Are oxygen concentrator machines sold or leased by the Taxpayer exempt from sales or lease tax as "drugs" pursuant to Code of Ala. 1975, 40-23-4.1;

(3) Should a portion of the lease payments received by the Taxpayer be excluded from taxable gross proceeds as nontaxable service or maintenance charges;

(4) Did the Taxpayer have sufficient nexus with the counties outside of Montgomery County so as to be subject to tax in those counties; and

(5) Should the Department be estopped from assessing the Taxpayer based on a letter sent by a Department employee to another durable medical equipment provider which erroneously stated that Medicare payments were not subject to sales tax.

The Taxpayer failed to file sales or lease tax returns during the period in issue. The Taxpayer claims that returns were not filed because it relied on a letter from a Department employee to another durable medical equipment provider stating in substance that amounts received from Medicaid or Medicare were not subject to Alabama sales tax. The Department audited the Taxpayer and assessed the tax in issue based primarily on the gross proceeds received by the Taxpayer from its Medicare patients. The parties agreed that because of the Taxpayer's voluminous records, the Department could conduct the audit using a sample period from January through June 1991. The Taxpayer does not dispute the

Department's audit method.

The Taxpayer does, however, dispute the assessments as follows:

(1) First, the Taxpayer contends that the gross proceeds received from Medicare are exempt from sales and lease tax. I disagree.

The above issue was previously decided by the Administrative Law Division in State v. Medical Care Equipment, Inc., Docket No. S91-221, decided on January 21, 1994. That case held that Medicare payments received from the sale or lease of durable medical equipment are subject to Alabama sales and lease tax. A similar conclusion was also reached in a Jefferson County Circuit Court case, Medical Oxygen and Equipment Service, Inc. v. State, CV82-503-615. A copy of the above decisions are attached to and made a part of this Opinion and Preliminary Order.

(2) The Taxpayer also argues that oxygen concentrator machines should be exempt from sales and lease tax as "drugs" pursuant to §40-23-4.1. That issue was also decided against the Taxpayer in the above cited Medical Care Equipment case, on page 3, as follows:

> Finally, the oxygen concentrator machines were not exempt under §40-23-4.1 because machines were not "drugs" as defined by that statute. The Taxpayer argues that the oxygen produced by the machines should be construed as a drug under §40-23-4.1. However, the item being taxed is the machine itself, not the oxygen that is dispensed by

> the machine. In any case, §40-23-4.1 applies to sales tax only. Thus, even if the machines were exempt from sales tax under §40-23-4.1, the machines would not also be exempt from rental tax.
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> Durable medical equipment was exempted from sales, use and lease tax by Act 93-353. However, Act 93-353 does not become effective until October 1994, and thus is not applicable in this case.

(3) The Taxpayer next argues that a part of the lease proceeds constituted nontaxble service and maintenance charges.

The Taxpayer was required by Medicare to periodically service all equipment leased to a Medicare patient. The Taxpayer also provided other services to patients not necessarily required by Medicare. The Taxpayer's patients were billed in a lump sum. That is, charges for service or maintenance of the equipment were not separately stated. Nonetheless, the Taxpayer argues that an estimated 40-50% of the Medicare proceeds should be allocated to non-taxable service or maintenance charges. I disagree.

"Gross Proceeds" for lease tax purposes is defined at Code of Ala. 1975, §40-12-220(4) as "the value proceeding or accruing from the leasing or rental of tangible personal property, without any deduction for . . . labor or service costs . . . or for any other expense whatsoever, . . ." The total amount received by the Taxpayer, including any service or maintenance charges included in the lump sum bill, constituted taxable gross proceeds under the above definition.

Department Reg. 810-6-5-.09.01(2) provides that a separate

contract for maintenance only is not taxable. However, there were no separate maintenance or service charges in this case.

(4) The Taxpayer also claims that it was not subject to tax in any county or municipality outside of Montgomery County because it did not have sufficient nexus with those jurisdictions. Again, I disagree.

The Due Process Clause of the U. S. Constitution requires that there must be "some definite link, some minimum connection between a state and the persons, property or transaction it seeks to tax". Miller Brothers v. Maryland, 347 US 340, 344-45. That minimum nexus requirement also applies to intrastate transactions. That is, a taxpayer can be subjected to a county or municipal tax only if the taxpayer has some minimum connection, i.e. nexus, with the taxing county or municipality.

The latest "definitive" U.S. Supreme Court case on the issue of nexus is Quill Corporation v. North Dakota By and Through Heitkamp, 112 S. Ct. 1904. In Quill, the Supreme Court ruled that for due process purposes actual physical presence by a taxpayer in a taxing jurisdiction is not necessary. Rather, sufficient nexus is achieved if the taxpayer "purposely avails itself of the benefits of a economic market in the forum (jurisdiction)". Quill, at 1910. Quill had no outlets, employees or other physical presence in North Dakota. Nonetheless, the Court held that Quill had sufficient nexus with North Dakota for due process purposes because

it regularly and systematically solicited business in North Dakota through catalogs, fliers, advertisements in national public periodicals, and by telephone.

In this case, the Taxpayer clearly availed itself of the economic market in the various counties and municipalities in issue. That alone is sufficient to satisfy the due process nexus requirement in Quill. In addition, the Taxpayer also had a physical presence because the Taxpayer made sales and leased property in those jurisdictions. The Taxpayer delivered its products into those counties and municipalities in its own vehicles. The Taxpayer also retained title to and its employees serviced the equipment that it rented in those jurisdictions. Clearly, the Taxpayer had sufficient nexus with the counties and municipalities in issue so as to be subject to sales and lease tax in those jurisdictions.

(5) The Taxpayer claims that the Department should be estopped from assessing the tax in issue because the Taxpayer relied in good faith on a letter from a Revenue Department employee to a local competitor indicating that durable medical equipment paid for by Medicare or Medicaid would be not be subject to sales tax. However, the Department cannot be estopped from collecting a tax that is properly due based on erroneous advice or information given by a Department employee. Boswell v. Abex, 317 So.2d 317. However, because the Taxpayer failed to timely file returns or pay

the tax in reliance on the erroneous letter, the failure to timely pay and file penalties included in the assessments should be waived.

The Department is directed to remove the penalties from the assessments and thereafter inform the Administrative Law Division of the adjusted amounts due. A Final Order will then be entered for the tax due plus interest. The Final Order when entered may be appealed to circuit court pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered on December 14, 1994.

BILL THOMPSON
Chief Administrative Law Judge