

STATE OF ALABAMA §
DEPARTMENT OF REVENUE, §

STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

vs.

MARY B. MONTGOMERY, d/b/a §
J. S. Montgomery Awards §
and Engraving §
310 Bell Building §
207 Montgomery Street §
Montgomery, AL 36104, §

DOCKET NO. S. 94-132

Taxpayer. §

FINAL ORDER

The Revenue Department assessed State and Montgomery County sales tax against Mary B. Montgomery ("Taxpayer"), d/b/a J. S. Montgomery Awards and Engraving, for the period March 1989 through January 1992. The Taxpayer appealed to the Administrative Law Division and a hearing was conducted on July 7, 1994. Alan E. Rothfeder represented the Taxpayer. Assistant counsel Wade Hope represented the Department.

The Taxpayer's husband, J. S. Montgomery ("Mr. Montgomery"), operated an engraving business and also sold plaques, trophies, awards, etc. at retail during the subject period. Mr. Montgomery was a skilled designer and hand engraver and specially designed and engraved some of the items sold at retail. The design and hand engraving charges were separately stated on the invoice to the customer. The issue in this case is whether the separately stated design and hand engraving charges constituted gross proceeds subject to sales tax.

The business maintained an inventory of ready-made plaques,

awards, etc., and also the materials necessary to make a special plaque or award if ordered by a customer. If a customer special ordered an item, Mr. Montgomery would design and hand engrave the item to the customer's satisfaction. The design and hand engraving charges were separately stated on the invoice issued to the customer. The Taxpayer collected sales tax on the tangible property, but not on the separately stated design and engraving charges.

The Department audited the Taxpayer, included the design and hand engraving charges as taxable gross proceeds, and based thereon entered the assessments in question. ¹

Sales tax is due on the gross proceeds derived from the retail sale of tangible personal property. Code of Ala. 1975, §40-23-2.

"Gross proceeds" is defined as "the value proceeding or accruing from the sale of tangible personal property . . . without any deduction on account of the cost of the property sold, the cost of the materials used, labor or service cost . . . or any other expenses whatsoever . . .". Code of Ala. 1975, §40-23-1(a)(6).

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The Department taxed the design and hand engraving charges only if the item was subsequently sold at retail. The Department agrees that hand engraving performed on an item provided by a customer was a non-taxable service.

In an attempt to clarify exactly what labor and service charges should be included in taxable gross proceeds, the Department promulgated Reg. 810-6-1-.84. That regulation reads as follows:

Receipts from labor or service necessarily or customarily performed incidental to the sale of property are a part of the gross proceeds of sales, either when included in the total charge or when billed as a separate item. Services not necessarily or customarily performed incidental to the sale of property or services unusual in nature and for which a separate and additional charge is made are not to be included in the gross proceeds of sales. (Readopted through APA Code effective October 1, 1982) (Section 40-23-1(6))

The Taxpayer argues that the design and hand engraving charges in issue should be excluded from taxable gross proceeds under Reg. 810-6-1-.84 because they constituted labor or services "unusual in nature". I disagree.

To begin, the statute defining "gross proceeds" must control, not the regulation that attempts to clarify the statute. Section 40-23-1(a)(6) requires that taxable gross proceeds must include the value proceeding or accruing from the sale of tangible personal property, without any deduction for labor or service costs. That is, all labor and service charges incidental to making or otherwise preparing the product for sale must be included in taxable gross proceeds.

The design and hand engraving in issue constituted labor or service performed by Mr. Montgomery in preparing the plaques, awards, etc. for sale. The labor or service was incidental to

preparing the items for sale, and thus must be included in taxable gross proceeds as defined at §40-23-1(a)(6).

The above holding is dispositive of this case. However, even under Reg. 810-6-1-.84, the design and hand engraving charges in issue would still be taxable.

The Taxpayer argues that the hand engraving was "unusual in nature" and thus should not be taxed under Reg. 810-6-1-.84 because it was unique to and could only be performed by Mr. Montgomery. However, the phrase "unusual in nature" must be read in the context of the retailer's business. That is, was the service or labor "unusual in nature" relative to the particular retailer in question. Hand engraving was not "unusual in nature" relative to Mr. Montgomery because he customarily and usually performed hand engraving in the normal course of his business. In other words, the design and hand engraving was "necessarily and customarily performed" by Mr. Montgomery and was not "unusual in nature" relative to his business so as to be excluded from tax even under Reg. 810-6-1-.84.

In any case, as discussed above, the taxability of labor or service charges does not hinge on whether the labor or service was "necessarily or customarily performed" by the seller, or was "unusual in nature". Rather, labor or service charges must be included in taxable gross proceeds under §40-23-1(a)(6) if incidental to making the product or preparing the product for sale, and if incurred or performed

prior to when the retail sale is closed (transfer of title). If so, then the service or labor is taxable, regardless of whether it is customarily performed or unusual in nature. In this case, the design and hand engraving was clearly performed by Mr. Montgomery in preparing the plaques, awards, etc. for sale. Consequently, the charges for that labor or service is taxable. The above considered, the final assessments in issue are affirmed. Judgment is entered against the Taxpayer for State sales tax of \$2,686.08 and Montgomery County sales tax of \$997.72.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g). Entered on December 29, 1994.

BILL THOMPSON
Chief Administrative Law Judge