Competitive Edge Office Systems, Inc.

Appellant,

vs.

The Sales Tax Board of Appeals

Appellee

Introduction

The Sales Tax Board of Appeals (Board) is an independent board appointed by the Assembly. CBJ 69.05.180. The purpose of the Board is to provide an appeal mechanism for controversies involving taxable sales, sales taxes, penalties, and interest that exceed five hundred dollars. As required under CBJ 69.05.180(b)(1), one member of the Board is an attorney, one is a CPA, and remaining members of the Board are members of the general public. Board members volunteer their time, knowledge, and experience with the Sales Tax Ordinance to hear appeals in a quasi-judicial process.

On October 19, 2001, Competitive Edge Office Systems, Inc., (CEOS), filed an appeal with the Sales Tax Board of Appeals. The subject of the appeal was an audit performed by the CBJ Sales Tax Office. The Board met on December 10, 2001, to hear the appeal. The Board reviewed written statements by both parties to the appeal and heard testimony from both sides. The Board found in favor of CBJ on both issues presented by CEOS. The Board issued a verbal notice of its decision on December 10, 2001, and followed this with a written decision on January 15, 2002, denying the appeal as to all issues.

Standard of Review

The written decision by the Board is the subject of CEOS’s appeal to the Assembly. CEOS has
the burden to prove that the Board erred in its decision.\(^1\) CEOS’ opening brief before the Assembly makes no argument that the appeals board’s decision was not supported by substantial evidence, was not supported by adequate written findings, or that the appeal board failed to follow its own procedures. In this appeal, CEOS has not met its burden.

**Background**

CEOS’s appeal is based on the Sales Tax Administrator’s determination, and the Board’s decision, that the commissions paid by Xerox and Herman Miller to CEOS were subject to sales tax. The Board found that services were being provided by CEOS to Xerox and Herman Miller, compensation was exchanged, and there was no exemption in the sales tax code, prior to November 15, 2001, for commissions. Therefore, the sales tax assessed on the commissions received by CEOS, was upheld by the Board. (R. 37).

CEOS asserts in its opening brief that the “city tax office” used the newly adopted exemption for commissioned sales agents as the reason that CEOS owes back tax in the audit. The Sales Tax Office informed CEOS on the taxability of its sales agent commissions at the beginning of the audit and assessed the tax due long before the commissioned sales agent exemption 69.05.040(40) was adopted. The Sales Tax Office did not use the commissioned sales agent exemption to determine the taxability of the commissions received by CEOS from Xerox and Herman Miller. However, as requested by CEOS in its appeal, the Board did consider the

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\(^1\)The CBJ appeals code provides:

01.50.070 Standard of review and burden of proof.
(a) The appeal agency or the hearing officer may set aside the decision being appealed only if:
   (1) The appellant establishes that the decision is not supported by substantial evidence in light of the whole record, as supplemented at the hearing.
   (2) The decision is not supported by adequate written findings or the findings fail to inform the appeal agency or the hearing officer of the basis upon which the decision appealed from was made; or
   (3) The appeal agency or the hearing officer failed to follow its own procedures or otherwise denied procedural due process to one or more of the parties.
(b) The burden of proof is on the appellant.
recently-adopted sales agent exemption when making its decision on the taxability of the services provided by CEOS to Xerox and Herman Miller prior to November 15, 2001. (R. 6).

This memorandum will address the issues brought forth by CEOS in its opening brief and show that the Board had opportunity to review and hear each issue.

Issues
1) CEOS asserts the commission it receives is “income.” (CEOS Brief, page 2). CBJ agrees the commission received by CEOS is income. However, it is not considered “unearned” or “passive” income. CEOS earns the commission by establishing a retail presence in CBJ to sell both Xerox and Herman Miller products. Individuals or businesses deciding to purchase either a Xerox or Herman Miller product in CBJ are directed to the local representative, CEOS, for its experience and knowledge about the products. CEOS states that it is the only representative for Xerox in Southeast Alaska. (R. 30).

CEOS provided an excellent overview of its business in the opening paragraph of its appeal to the Board.

The Competitive Edge is a well-established Juneau business that acts as the local agent for national companies Xerox and Herman Miller. Their business is to support the regional business clients of Xerox and Herman Miller, who are the primary vendors for The Competitive Edge. The work of The Competitive Edge involves maintaining contacts with businesses and government agencies providing continuity with the company and obtaining sales orders which are completed by the Xerox and Herman Miller offices out of state. Both Xerox and Herman Miller pay [SIC] sales tax on the transaction. Competitive Edge is not a
party to the transaction except for relaying the order to the central office. Competitive Edge receives a commission on the transaction. (R. 4)

CEOS operates as an “agent” for Xerox and Herman Miller; CEOS obtains sales orders completed by Xerox and Herman Miller; CEOS relays the order to the central office and receives a commission on the transaction. Because CEOS provides a service to Xerox and Herman Miller as defined by the Sales Tax Code, and because services performed within the CBJ are taxable, the decision of the Sales Tax Administrator and the Sales Tax Board of Appeals should be upheld. CEOS provided a taxable service, prior to the adoption of Exemption 40.

CEOS made the decision to become an “agent” for Xerox and Herman Miller rather than a “dealer.” A “dealer” would purchase the product up front, maintain an inventory, and the dealer’s business profit would be based on the additional amount the product could be sold for, over and above its cost. An agency status by definition would authorize CEOS to function as a representative of both Xerox and Herman Miller and to act on their behalf in obtaining sales orders for their products. Once a sales order is obtained, CEOS remits this order to Xerox or Herman Miller. Xerox and Herman Miller deliver the product to the customer and bill the customer directly. In return for securing the sales order for Xerox and Herman Miller, CEOS receives a commission on the sale (based as a percentage of the selling price of the product order). (R. 4). An “agent” does not purchase the product up front or maintain an inventory; the agent’s profit is based on a commission earned on sales output. (R. 26). All businesses make choices when establishing business practices, and some choices have tax consequences. The choice to be an “agent” rather than a “dealer” has a sales tax consequence.
In compliance with the CBJ Sales Tax Ordinance, CEOS should have collected sales
tax on the commissions it receives from Xerox and Herman Miller. Any failure by
CEOS to collect the sales tax from Xerox and Herman Miller does not make such
sales exempt from the sales tax.\(^2\)

2) CEOS asserts that its commission income is subject to both State and Federal
income taxes. (CEOS Brief, page 3). It is the understanding of the Sales Tax Office
that for-profit corporations conducting business in Alaska are subject to both Federal
and State income tax on net taxable earnings, regardless of whether the income is
earned by performing a service, making retail sales, or rentals. The Sales Tax Office
is not sure what point CEOS is attempting to make with this statement. The fact that
CEOS may or may not pay other taxes does not make its transactions exempt from the
CBJ sales tax. This issue was presented to the Board. (R. 6).

3) CEOS claims CBJ’s interpretation of a service is “very wide-reaching and fuzzy.”
(CEOS Brief, page 3). CEOS does not own the Xerox and Herman Miller product;
CEOS has stated the product sale is made directly by Xerox and Herman Miller. (R.
31). CBJ 69.05.010 defines services as “all services of every manner and description
that are performed or furnished for consideration whether in conjunction with the sale
of goods or not...” The code definition of a service is very broad, and the code
further requires that the Sales Tax Administrator interpret the levy of the tax broadly.

\(^2\) 69.05.070 (b) The tax levied under this chapter, whether or not collected from the buyer,
except for credit transactions covered in subsection (c) of this section, must be remitted by the
seller to the City and Borough at the time of transmitting the return, and if not so remitted or if the
return is not timely filed, such tax is delinquent. (Emphasis added).
In oral arguments before the Sales Tax Board of Appeals, CEOS stated the following:

"I could see it would be a service if Xerox paid us a flat rate amount for representing them here in Juneau . . . " (R. 18). "Or if Xerox paid us $2,000 a month just base, without, you know, doing anything or selling anything in Juneau, I could see that as a service." (R 25).

CEOS agrees that it would be providing a (taxable) service if the method of payment was different. The method of payment, agreed to by the parties to the transaction, does not alter the basic business transaction. CEOS is providing a service to Xerox and Herman Miller and CEOS receives consideration for the service. A method of payment does not change the sale from a sale of a service to income not subject to the CBJ sales tax. The Sales Tax Administrator and the Appeals Board found that the services to Xerox and Herman Miller for which CEOS was paid a commission clearly fell within the definition of "services" under the Sales Tax Ordinance. (R. 44).

4) CEOS asserts Xerox and Herman Miller are suppliers for CEOS "only." (CEOS Brief, page 3). CEOS does operate as a "dealer" for some products such as fax machines. CEOS purchases these products and maintains an inventory. (R. 27). In this capacity Xerox is considered a supplier. CEOS does not dispute the taxability of these sales of goods.

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3 69.05.005 It is the purpose of the tax levied under this chapter to raise revenues. To that end, the scope of the tax levied shall be broadly interpreted and exemptions shall be allowed only when the rental, sales or service clearly falls within an exemption defined in this chapter.
However, in relation to the photocopiers sold, for which CEOS receives a
commission, CEOS is not a party to the transaction except for taking orders. (R. 4).
CEOS does not own the photocopier products sold. (R. 31). CEOS does not maintain
a photocopier inventory. (R. 29). Xerox and Herman Miller are not photocopier
“suppliers” for CEOS.

The Sales Tax Office is not sure of CEOS’ point in 4) in relation to the tax law. CBJ
69.05.020 levies the sales tax on retail sales, services performed and rentals made. As
previously stated, CBJ 69.05.010 defines services as “all services of every manner
and description that are performed or furnished for consideration whether in
conjunction with the sale of goods or not . . . .” CEOS is the local agent for Xerox and
Herman Miller. (R. 4). The commission received by CEOS is subject to the levy of
the sales tax.

5) CEOS contends that the sales agent commission exemption 69.05.040(40) was
adopted to clarify the vague tax code and prevent the City from incorrectly taxing
income. (CEOS Brief, page 3). The sales tax code does not levy the sales tax on
“income” but levies the sales tax on the selling price. The Assembly could have
exempted all sales agents commissioned sales. It did not do so. The sales agent
commission exemption, 69.05.040(40), adopted by the Assembly excludes sales
agent commissions on the sale of real property.

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4 69.05.020 Imposition of rate.
   (a) There shall be levied and collected a tax equal to the percentage of the selling
   price on retail sales and rentals made and services performed within the City and
   Borough as follows:

5 69.05.040(40) The commission paid to an agent for negotiating the sale or lease of tangible
   personal property on behalf of the owner of the property provided that the
   commission is the only compensation paid to the agent for negotiating the sale.
The adoption of the sales agent commission exemption, 69.05.040(40), would signify that the Assembly’s intent was to exempt only certain customers, utilizing a sales agent, from the payment of the sales tax on its purchase of a service. A sales agent, excluding a sales agent for real property sales, operating on a commissioned basis would not be required to collect the sales tax on its commission sales since the adoption of the exemption.

A real estate agent that sells on a commission basis is still required to collect the sales tax on its commission sales. (R. 35). In fact, CEOS commissioned sales are almost exactly like that of a real estate agent. A real estate agent does not own the product/property sold, does not have the ability to pass title, and only secures the agreement of a willing buyer and a willing seller. For its services, a real estate agent is paid a commission when the sale is complete. The real estate agent adds the sales tax to the commission and collects the sales tax from its customer. In comparing the business practices of CEOS to a real estate agent, the basic transactions are the same.

CEOS has asserted that the difference between the services provided by a real estate agent and the services it provides would be that the majority of the sales on which a commission is earned by a real estate agent would be exempt from the sales tax. (R.35). However, CEOS has stated that the majority of the sales made by Xerox and Herman Miller are to exempt government entities. (R. 5). CEOS may argue that the differences are the sale of real property versus tangible personal property, the business practices are the same. The difference that now exists, after the adoption of Exemption 40, is future commissions paid by Xerox and Herman Miller are exempt from the sales tax while the commissions paid by an individual selling a home remain subject to the sales tax. (R. 19).
CEOS asserts that the City has never taxed its particular commission structure in the ten years it has been representing Xerox in Juneau. (CEOS Brief, page 3). In audit, CBJ determined CEOS had excluded its commissions from gross sales when reporting on its sales tax return. CEOS did not seek the advice of its attorney, CPA, or the Sales Tax Office to determine if this was correct. (R. 24)

The fact that CEOS did not comply with the Sales Tax Ordinances does not mean that the tax structure was not in place or that this type of commission structure was never taxed. Agents have been collecting and reporting the sales tax on their commissioned sales for well beyond the ten years that CEOS has been in business.

6) CEOS discusses the process of the adoption of CBJ Sales Tax Exemption 69.05.040(40), and the estimation process of the impact by city officials. A sales commission is a method of payment, not an industry. A business does not report the method in which it is paid when reporting to the sales tax office. The difficulties in estimating the impact were presented by the city officials. This issue was presented to the Board for its consideration in making its decision. (R.19). The Sales Tax Office consistently strives to provide the Assembly with the best information available to make tax policy decisions. The Sales Tax Office constantly counsels merchants on the importance of reporting sales and exemptions appropriately. However, if merchants, exclude information from gross sales, and fail to report exemptions appropriately, the information provided will never be totally accurate.

The Sales Tax Office understands CEOS’ concern over the amount of time taken to complete the audit findings. There was a delay in completing the audit. The sales tax office has apologized to CEOS. In addition, the Sales Tax Administrator stopped the
interest accrual on the additional tax due, assessed as of December, 2000, to the date
of the final audit findings. Interest continues to accrue on the unpaid tax balance from
the date of the final audit findings letter to the present. The Sales Tax Office has put
procedures into place that will help prevent delays in the completion of future sales
tax audits.

CEOS quotes in its conclusion the last sentence of 69.05.180(b)(3) “The assembly may, by
motion or resolution, modify any rules adopted by the board.” CBJ 69.05.180(b)(3) grants
authority to the Sales Tax Board of Appeals to adopt rules of procedure that would govern
the sales tax appeals and the proceedings before the Board. The procedures adopted by the
Board are submitted to the Assembly for approval. The above quoted sentence by CEOS
allows the Assembly to modify the rules of procedure the Board may have adopted.

If CEOS is asking the Assembly to overturn the decision by the Board when it found in favor
of CBJ, the method to overturn the decision of the Board is found in CBJ appeals code
01.50.070, and the burden is placed on the Appellant, CEOS.

Conclusion

The CBJ Sales Tax Code is very broad and requires the Sales Tax Administrator to
interpret the levy of the tax broadly. The levy is placed on the sale of all goods,
services, and rentals unless specifically exempted. Exemptions to the sales tax are
allowed only when a transaction clearly falls within the exemption definitions of CBJ
69.05. In all instances the Sales Tax Administrator must first look at the transaction
and then the law.

CEOS does not own the products sold. (R. 31). CEOS does not maintain an
inventory. (R. 29). “Competitive Edge is not a party to the transaction except for relaying the order to the central office. Competitive Edge receives a commission on the transaction.” (R. 4).

CEOS does not sell a product. The Sales Tax Administrator has determined that CEOS provides a service to Xerox and Herman Miller, and CEOS receives consideration from Xerox and Herman Miller in the form of a commission, as defined in CBJ 69.05.010.

CBJ 69.05 exempts from the sales tax commissions earned by Insurance Agents (69.05.040(2)), Travel Agents (69.04.040(24)), and Investment Bankers (69.05.040(26)). Prior to November 15, 2001, an exemption for sales agent commissions, for transactions similar to those of CEOS, did not exist in CBJ 69.05. CBJ did determine that the service provided by CEOS to Xerox would qualify for the “cap” on the sale of a single service.⁶ The commissions received from Herman Miller did not exceed the “cap” amount in any one month of the audited periods. The amount of tax due, in audit, was reduced by the Sales Tax Administrator’s finding that the Xerox transactions would qualify for the “cap” on the sale of a single service. (R. 21).

In audit, CBJ determined that CEOS was not reporting commissions on its sales tax returns. CBJ reviewed the transaction, determined that a service was being provided,

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⁶69.05.040(22) That part of the periodic selling price of a single service that exceeds $7,500.00. The periodic selling price is the amount owed on a calendar month or invoice basis, whichever is more frequent. Services or contracts exceeding a payment period of one calendar month are computed for sales tax purposes as though payment were to be made on a calendar month basis. A single service is an interrelated and interdependent function necessary to perform a specified action.
and compensation was exchanged, and billed the tax due as required in CBJ 69.05.

As required, under the rules of procedure adopted by the Sales Tax Board of Appeals:

1) CEOS filed an appeal of the determination of the Sales Tax Administrator to the Sales Tax Board of Appeals within the 20-day deadline. 2) The Sales Tax Administrator filed a written statement outlining CBJ’s position. 3) The Appeals Board held a hearing and heard testimony from both parties. 4) The Appeals Board issued a verbal notice of its decision and followed with a written decision providing the basis for its findings. The Appeals Board found in favor of CBJ on both issues.

In this appeal, CEOS has not met its burden. Therefore, the determination by the Sales Tax Administrator and the Sales Tax Board of Appeals should be upheld.

Dated this 8th day of May, 2002.

[Signature]

CBJ Sales Tax Board of Appeals

Joan Roomsburg
Sales Tax Administrator