OHIO BOARD OF TAX APPEALS

KARVO PAVING CO., (et. al.),

Appellant(s),

vs.

JOSEPH W. TESTA, TAX COMMISSIONER OF OHIO, (et. al.),

Appellee(s).

CASE NO(S). 2016-782

(USE TAX)

DECISION AND ORDER

APPEARANCES:

For the Appellant(s) - KARVO PAVING CO.
Represented by:
STEVEN A. DIMENGO
BUCKINGHAM, DOOLITTLE & BURROUGHS, LLC
3800 EMBASSY PARKWAY, SUITE 300
AKRON, OH 44333

For the Appellee(s) - JOSEPH W. TESTA, TAX COMMISSIONER OF OHIO
Represented by:
DANIEL W. FAUSEY
ASSISTANT ATTORNEY GENERAL
OFFICE OF OHIO ATTORNEY GENERAL
30 EAST BROAD STREET, 25TH FLOOR
COLUMBUS, OH 43215-3428

Entered Thursday, January 4, 2018

Mr. Harbarger, Ms. Clements, and Mr. Caswell concur.

This matter is now considered upon appellant's notice of appeal from a final determination of the Tax Commissioner, the statutory transcript ("S.T.") certified by the commissioner, the record of the hearing ("H.R.") before this board, and the parties' written arguments.

Appellant, Karvo Paving Co. ("Karvo") was assessed use tax following audit of its purchases from January 1, 2008 through June 30, 2013. Karvo objected to the assessment through a petition for reassessment, and the commissioner denied its objections and Karvo appealed to this board. Although it specified eight separate errors in its notice of appeal, at hearing and in its written legal argument, Karvo focuses on three categories of assessed items: (1) "traffic maintenance property," i.e. barrier walls, barricades, temporary traffic lights, message boards, and signs, (2) employment services provided by K&H Excavating ("K&H"), and (3) equipment leased from K&H.

We acknowledge that the findings of the Tax Commissioner are presumptively valid. *Alcan Aluminum Corp. v. Limbach*, 42 Ohio St.3d 121 (1989). It is incumbent upon a taxpayer challenging a decision of the Tax Commissioner to rebut the presumption and establish a clear right to the relief requested. *Kern v. Tracy*, 72 Ohio St.3d 347 (1995); *Ball Corp. v. Limbach*, 62 Ohio St.3d 474 (1992); *Belgrade Gardens v.*

Kosydar, 38 Ohio St.2d 135 (1974). The burden is on the taxpayer to present credible evidence to support its claim that an assessment is in error. *Kern*, supra; *May Co. v. Lindley*, 1 Ohio St.3d 6 (1982); *Federated Dept. Stores v. Lindley*, 5 Ohio St.3d 213 (1983).

Pursuant to R.C. 5739.02, an excise ("sales") tax is levied upon all retail sales made in Ohio. By virtue of R.C. 5741.02, a corresponding tax is imposed on the storage, use, or consumption in this state of any tangible personal property. The legislature has also provided numerous exceptions and exemptions to the collection of sales tax, and, through R.C. 5741.01(C)(2), has mandated that if acquisition of an item within the state would not be subject to tax, then the item's use within the state is correspondingly not subject to tax. However, "[s]tatutes relating to exemption or exception from taxation are to be strictly construed, and one claiming such exemption or exception must affirmatively establish his right thereto." *Natl. Tube Co. v. Glander*, 157 Ohio St. 407 (1952), paragraph two of the syllabus. See also *Ball Corp.*, supra.

Karvo is a paving/construction contractor. A substantial portion of Karvo's contracts are with the Ohio Department of Transportation ("ODOT") and other political subdivisions in Ohio for paving/repaving existing roads. H.R. at 13-14, Ex. I. As part of the ODOT bidding and contract process, Karvo is required to bid and, if selected as the contractor, provide, traffic maintenance equipment to be used in directing, controlling, and informing traffic. During the project, an on-site ODOT engineer directs the use and placement of such traffic maintenance equipment. Id. at 26-28. Due to the control exercised by ODOT with regard to the equipment, Karvo argues that ODOT has possession of the property, thereby excepting it from use taxation under R.C. 5739.01(E). Under that section, a "retail sale" to which the sales/use tax applies, is defined as *excluding* those sales "in which the purpose of the consumer is to resell the thing transferred ***, by a person engaging in business, in the form in which the same is, or is to be, received by the person." R.C. 5739.01(B)(1) further defines "sale" as including "[a]ll transactions by which title or possession, or both, of tangible personal property is or is to be transferred ***." Karvo argues that, pursuant to its contracts with ODOT, it transfers possession of the traffic maintenance equipment in the same form in which it receives it, and therefore is not liable for use tax on such items. The commissioner argues in response to that the traffic maintenance equipment is taxable under Ohio Adm. Code 5703-09-14(H) as "property purchased or leased by a construction contractor and used or consumed in performing a construction contract."

We agree with Karvo's contention. As the Supreme Court explained in *Dresser Industries, Inc. v. Lindley*, 12 Ohio St.3d 68 (1984), in analyzing a claim of exception from sales/use tax as a purchase for resale, we must look to the *purchaser's* primary use of the property. The traffic maintenance equipment is not used by Karvo in performing the paving work it performs. It essentially rents the equipment to its customer – ODOT – to allow ODOT to maintain traffic during Karvo's work, in accordance with ODOT's own obligations. While we acknowledge the commissioner's argument that the equipment does provide some benefit to Karvo by ensuring the safety of its workers during the project, Karvo has no say in choosing the type of equipment it feels could most efficiently ensure the safety of its workers. For example, George Karvounides, owner of Karvo, testified that, in lieu of using a barrier wall, Karvo could use barrels or work in a smaller area. H.R. at 22. The ODOT contract bid documents specify the size, type, and amounts of such equipment, and the on-site ODOT engineer controls the placement and use of the equipment. H.R. at 27-28, Exs. IV, V. While part of its contract with ODOT, the equipment is not used or consumed in performing Karvo's paving duties under the contract, other than by providing the equipment for ODOT's use, under ODOT's direction. We therefore find that the traffic maintenance equipment is not taxable under Ohio Adm. Code 5703-09-14(H), but, rather, is excepted from taxation under R.C. 5739.01(E).

Karvo also challenges personnel/services and equipment leased from a related entity, K&H. Mr. Karvounides testified that, in 2000, Karvo purchased the assets of an existing company, Wayne Herbruck Excavators ("Herbruck"), owned by Wayne Herbruck, through another related Karvo entity – Karvo 5 Ltd. (now dba K&H Excavating, LLC) (herein referred to as "K&H"). H.R. at 67-68. Karvo 5 is owned 55% by Mr. Karvounides' wife, Ana, and 45 percent by himself. Id. at 70. After the acquisition, K&H continued to do site work excavation using its then-existing 15-20 employees, sometimes using Karvo as its

paving subcontractor. Id. at 73-75. In 2007, K&H ceased doing private work. The mechanics who had been employed by K&H continued to be employed by K&H, and performed maintenance work on Karvo's equipment. Id. at 85-86. Mr. Karvounides testified that the only business in which K&H was engaged after 2007 was leasing excavators and bulldozers to Karvo. Id. at 77. The revenue derived by K&H from its leasing transactions was used to meet Karvo's financial obligations to Mr. Herbruck under its purchase agreement. Id. at 80. In addition, K&H continued to employ mechanics, who performed maintenance work for Karvo at Karvo's business location/shop, and another related company, Karvo Trucking. The mechanics were supervised by Mr. Karvounides' brother, Gus, who is employed by Karvo Paving and is also an owner of Karvo Trucking. Id. at 85-86.

The commissioner assessed Karvo use tax on repair/employment services provided by K&H. Karvo first argues that the transactions are not taxable as transactions between members of an affiliated group under R.C. 5739.01(JJ)(4). Mr. Karvounides testified at hearing that he and his wife are the owners of both Karvo and K&H, and that, pursuant to an agreement dated September 19, 1997, he has complete authority over the business matters of Karvo 5 Ltd. dba K&H Excavating, LLC. H.R., Ex. XI. Karvo further argues that, pursuant to Tax Commissioner Opinion 93-0012, entities owned by a husband and wife are affiliated.

R.C. 5739.01(JJ)(4) excludes from the definition of "employment service" "[t]ransactions between members of an affiliated group." R.C. 5739.01(B)(3)(e) further defines "affiliated group" as "two or more persons related in such a way that one person owns or controls the business operation of another member of the group ***." It is clear from the record that Karvo Paving and K&H were controlled by Mr. Karvounides. Although the commissioner denied Karvo's argument below on this point, he indicated he did so based on a lack of any evidence to support the contention. Mr. Karvounides' credible testimony, together with the September 1997 agreement, provides sufficient evidence of his control over both entities. As such, we agree with Karvo that the transactions by which K&H provided mechanics to Karvo were not taxable, as transactions between members of an affiliated group. As such, we need not reach Karvo's alternate argument that the transactions are exempt as permanent assignment of leased employees under R.C. 5739.01(JJ)(3).

Finally, Karvo argues that leases of equipment from K&H to Karvo should be exempt as "casual sales" under R.C. 5739.02(B)(8). Under R.C. 5739.01(L), a "casual sale" is "a sale of an item of tangible personal property that was obtained by the person making the sale *** for the person's own use and was previously subject to any state's taxing jurisdiction on its sale or use ***." Karvo argues that, prior to its acquisition of Herbruck through Karvo 5 Ltd. in 2000, Herbruck had purchased the excavators and bulldozers in question for its own use in its site excavation business; its subsequent leases of that equipment to Karvo were therefore exempt as casual sales. In response, the commissioner argues that K&H's sole business was leasing equipment, rendering none of its leases "casual." Moreover, the commissioner argues that there is no concept of "casual *leases*" in Ohio law, citing the code's separate definition of "lease" in R.C. 5739.01(UU), and that Karvo has failed to submit any evidence that sales tax was previously paid upon the purchase of the equipment in question as required by R.C. 5739.01(L).

We agree with the commissioner. The record demonstrates that the only business conducted by K&H during the period in question was leasing equipment. H.R. at 80-81. It therefore cannot be said that the leases were casual. Karvo brought about this factual situation by retaining K&H as a separate entity and operating it solely as a leasing business; it cannot "take the benefits arising from having two corporations and at the same time escape the hazards." *Union Building & Const. Corp. v. Bowers*, 110 Ohio App. 81, 87 (1958). We therefore find that the transactions do not qualify as casual sales under R.C. 5739.01(L).

Although Karvo raised five additional errors in its notice of appeal, as noted by the commissioner, no further argument or evidence has been provided on those errors. As such, we find that appellant has failed to meet its burden on those points, to the extent they have not been abandoned.

Based upon the foregoing, we find that appellant has failed to meet its burden of proof related to leased

property, and therefore affirm the commissioner's final determination as to those items. However, we do find that appellant has met its burden with regard to the traffic maintenance equipment and employment services. Accordingly, we reverse the determination of the Tax Commissioner on the assessed traffic maintenance equipment and employment services.

BOARD OF TAX APPEALS		
RESULT OF VOTE	YES	NO
Mr. Harbarger		
Ms. Clements		
Mr. Caswell		

I hereby certify the foregoing to be a true and complete copy of the action taken by the Board of Tax Appeals of the State of Ohio and entered upon its journal this day, with respect to the captioned matter.

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Kathleen M. Crowley, Board Secretary