IN THE DISTRICT COURT OF LANCASTER COUNTY, NEBRASKA

ENTERPRISE RENT-A-CAR COMPANY-MIDWEST, LLC,	)	**Case No. CI 11-3101**
Plaintiff/Appellant,	)	
vs.	)	**ORDER**
NEBRASKA DEPARTMENT OF REVENUE, AGENCY OF THE STATE OF NEBRASKA, and DOUGLAS A. EWALD, TAX COMMISSIONER	)	
Defendants/Appellees.	)	

This matter was before the court on May 15, 2012, for hearing on the appeal of a final decision of Douglas A. Ewald, Tax Commissioner, denying a Petition for Redetermination of a deficiency assessment for Nebraska sales tax issued by the Nebraska Department of Revenue ("Department") to Appellant Enterprise Rent-A-Car Company-Midwest, LLC ("Enterprise"). Attorney Thomas J. Kenny appeared on behalf of Enterprise and Assistant Attorney General L. Jay Bartel appeared on behalf of the Department and the Tax Commissioner. The certified Transcript and volumes I and II of the Bill of Exceptions were received. The matter was argued, briefed and submitted. The issue on appeal is whether certain charges associated with the lease of a vehicle (specifically Damage Waiver fees, and refueling service charges) are subject to sales tax under Nebraska law. The court now finds and orders as follows:

LANCASTER COUNTY
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DISTRICT COURT

FACTS

The parties' stipulated facts are contained in the Stipulation of Facts & Issues & Exhibit List received in evidence at the administrative hearing (Ex. 1), and the facts are not in dispute. Enterprise operates a motor vehicle leasing business at several locations in Nebraska. (Ex. 1, ¶¶1, 4). The Department conducted an audit of Enterprise's books and records to determine its liability for sales, consumer's use, and other taxes and fees for the period January 1, 2004 through August 31, 2007. (Ex. 1, ¶6). Following the audit, the Department issued a Notice of Deficiency Determination ("Notice") to Enterprise reflecting a sales and consumer's use tax liability for the audit period in the amount of $436,068.00, consisting of $339,824.00 tax, $62,261.00 interest, and $33,983.00 penalty. (Ex. 1, ¶7). Enterprise timely petitioned for redetermination of the Notice and, upon further review, the Department reduced the proposed assessment to $350,609.57. (Ex. 1, ¶¶8–13, 15). The remaining sales tax subject to the deficiency assessment ($250,577) reflects sales tax which Enterprise failed to collect and remit on two optional charges imposed on certain customers as part of the Lease Agreement: Optional Damage Waiver charges, and refueling charges. (Ex. 1, ¶¶14, 16).

Optional Damage Waiver

Enterprise's Standard Form Lease Agreement (Ex. 4) includes provisions requiring customers to mark and initial a box evidencing whether they "decline" or "accept" the Optional Damage Waiver when leasing a vehicle. (Ex. 1 ¶18; Ex. 4 p.1) The Lease Agreement specifically recites that "THE PURCHASE OF DAMAGE WAIVER IS OPTIONAL AND NOT REQUIRED IN ORDER TO RENT A VEHICLE." (Ex. 1, ¶¶18, 19; Ex. 4, ¶16). If a customer accepts the Optional Damage Waiver ("Damage Waiver"), Enterprise agrees to contractually

waive the customer's damage responsibility for all of the costs of damage to, loss, or theft of the vehicle or any part or accessory and related costs regardless of fault or negligence. (Ex. 1, ¶20). If a customer accepts the Damage Waiver and the rented vehicle sustains damage during the rental period, Enterprise may elect to repair the vehicle depending on the amount of the damage the vehicle sustained and the applicable salvage laws. (Ex. 1, ¶21). If a repair is done on a vehicle for which a customer accepts the Damage Waiver when entering into the Lease Agreement, then Enterprise pays the cost to repair the vehicle. (Ex. 1, ¶22). Customers who decline the Damage Waiver agree to accept responsibility for damage to, loss, or theft of the vehicle. (Ex. 4, p.4, ¶¶3.d.(2) and 6.). Enterprise records the amounts associated with the Damage Waiver in a separate account. (Ex. 1, ¶23).

Refueling Charges

The Lease Agreement also requires customers to choose one of two refueling options. (Ex. 1, ¶24). The first refueling option allows the customer to "pre-pay" a charge based on the fuel level of the vehicle at the time of the rental ("Fuel Option 1"). (Ex. 1, ¶25). Under Fuel Option 1 customers are not charged for fuel upon the return of the vehicle, regardless of the fuel level at the time the vehicle is returned. (Ex. 1, ¶25). Under the second refueling option, called the "post-pay" option, the fuel tank level is assessed at the time of the rental and the customer is either (1) not charged if the fuel level is the same or higher when the vehicle is returned or (2) is assessed a fueling service charge if the fuel tank is at a lower level upon return of the vehicle ("Fuel Option 2"). (Ex. 1, ¶26). Under Fuel Option 2 customers are free to choose whether to (1) refuel the vehicle at the customer's own expense prior to returning the vehicle or (2) not refuel the vehicle and pay the refueling charge at the time the vehicle is returned. (Ex. 1, ¶27).

Enterprise records the amounts associated with the refueling charge in a separate account. (Ex. 1, ¶28).

Enterprise and the Department stipulated that the issue to be resolved by the Tax Commissioner was "whether under Nebraska law, (1) damage waiver fees and/or (2) fueling service charges associated with the lease of a vehicle are subject to sales tax." (Ex. 1, p.7). Following a hearing before a designated hearing officer on Enterprise's Petition for Redetermination, the Tax Commissioner entered an Order denying the Petition and declaring the deficiency assessment due and payable. (T30–32). The Tax Commissioner found that, because a customer must choose whether or not to pay the Damage Waiver and refueling charges at the time the lease transaction takes place, both charges are "necessary parts of the lease and any receipts attributable to them are subject to the tax." (T32).

STANDARD OF REVIEW

This is an appeal pursuant to NEB. REV. STAT. §§ 77-27,127, 77-27,128 (Reissue 2009), and 84-917 (Cum. Supp. 2010). When reviewing the final decision of an administrative agency pursuant to the Administrative Procedure Act, the district court conducts the review without a jury *de novo* on the record of the agency. NEB. REV. STAT. § 84-917(5)(a); *Betterman v. State of Neb. Dep't of Motor Vehicles*, 273 Neb. 178, 191, 728 N.W.2d 570, 584 (2007). The meaning and interpretation of statutes and regulations are questions of law for which a reviewing court has an obligation to reach an independent conclusion irrespective of the decision made below. *Mahnke v. State*, 276 Neb. 57, 61, 751 N.W.2d 635, 640 (2008). The district court may affirm, reverse, or modify the decision of the agency or remand the case for further proceedings. NEB. REV. STAT. § 84-917(6)(b).

ANALYSIS

Enterprise contends the Tax Commissioner erred as a matter of law by denying Enterprise's petition for redetermination of sales tax and by holding that any receipts attributable to the Damage Waiver and refueling charges are subject to the Nebraska sales tax. Enterprise argues the Damage Waiver and refueling charges imposed on customers under the Lease Agreement are not part of the "gross receipts" from the lease of vehicles subject to sales tax because these are optional charges which are not part of the price of the lease and are separable from the rental of the vehicle. In contrast, The Department maintains that Damage Waiver charges and refueling charges are part of the total consideration paid by Enterprise customers to rent vehicles under the Lease Agreement, and properly are included in the "gross receipts" from the lease or rental price of the vehicles that are subject to Nebraska sales tax. Upon consideration of the entire record, the court agrees with the Tax Commissioner's decision that the Damage Waiver charges and refueling charges are included in the "gross receipts" from the lease of vehicles and are, therefore, subject to sales tax.

The Damage Waiver Charges and Refueling Charges are Properly Included in Nebraska's Statutory Definition of "Gross Receipts"

Nebraska "impose[s] a tax . . . upon the gross receipts from all sales of tangible personal property sold at retail in this state." NEB. REV. STAT. § 77-2703(1) (Supp. 2011).[1] "Retail sale or sale at retail means any sale, lease, or rental for any purpose other than for resale, sublease, or subrent." NEB. REV. STAT. § 77-2701.31 (Reissue 2009). "Gross receipts means the total amount of the sale or lease or rental price, as the case may be, of the retail sales of retailers." NEB. REV.

[1] Citations to the Nebraska Revised Statutes refer to the current iteration of each statute. The operative language for purposes of this appeal are unaffected by any amendments during the relevant time period.

STAT. § 77-2701.16(1) (Reissue 2009). "Lease or rental means any transfer of possession or control of tangible personal property for a fixed or indeterminate term for consideration." NEB. REV. STAT. § 77-2701.18(1) (Reissue 2009). "In the rental or lease of automobiles, . . . the tax shall be collected by the lessor on the rental or lease price . . . ." NEB. REV. STAT. § 77-2703(1)(g). "Sales price applies to the measure subject to sales tax and means the total amount of consideration, including cash, credit, property, and services, for which personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise . . . ." NEB. REV. STAT. § 77-2701.35(1) (Reissue 2009). "Sales price" is determined "without any deduction for . . . (c) Charges by the seller for any services necessary to complete the sale." NEB. REV. STAT. § 77-2701.35(1)(c).

"In the absence of anything to the contrary, statutory language is to be given its plain and ordinary meaning," and a "court will not resort to interpretation to ascertain the meaning of statutory words that are plain, direct, and unambiguous." *Japp v. Papio-Missouri River Natural Res. Dist.*, 271 Neb. 968, 973, 716 N.W.2d 707, 711 (2006). The plain language of the relevant statutes provides that "gross receipts" subject to sales tax includes "the total amount of consideration . . . for which personal property . . . [is] leased, or rented," which, in the case of the lease or rental of automobiles involving the "transfer of possession or control" of a vehicle "for a fixed or indeterminate term for consideration," is "collected by the lessor on the rental or lease price." NEB. REV. STAT. §§ 77-2701.35(1); 77-2701.18; and 77-2703(1)(g).

Enterprise contends "gross receipts" only includes that consideration which causes transfer of possession of the vehicle, and because a customer can opt not to pay the Damage Waiver and refueling charges and still rent the vehicle, Enterprise argues those charges are not part of the sales

or lease price of the vehicle and should not be included in "gross receipts" subject to the sales tax. The court finds Enterprise's reading of the plain language of the sales tax statutes too narrow. "Sales price" is defined broadly as:

> the total amount of consideration, including cash, credit, property, and services, for which personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise, without any deduction for the following:
>
> (a) The seller's cost of the property sold;
>
> (b) The cost of materials used, the cost of labor or service, interest, losses, all costs of transportation to the seller, all taxes imposed on the seller, and any other expense of the seller;
>
> (c) Charges by the seller for any services necessary to complete the sale;
>
> (d) Delivery charges; and
>
> (e) Installation charges.

NEB. REV. STAT. 77-2701.35(1). The inclusion of charges for delivery, installation, and "any other expense of the seller" when computing the sales price subject to sales tax indicates the Legislature intended to include all consideration paid for the sale or rental of tangible personal property, including those items incidental to the actual transfer of possession of the property.

This reading of the sales tax statutes finds support in the Nebraska Supreme Court's decision in *Omaha Public Power Dist. v. Nebraska State Tax Comm'r*, 210 Neb. 309, 314 N.W.2d 246 (1982). In that case, Omaha Public Power District (OPPD) was assessed a sales and use tax deficiency on management fees and loss reimbursement payments paid by OPPD to a food service provider, Saga, with whom OPPD contracted to provide food service on OPPD's premises to its employees. The district court found the management fees and loss reimbursement payments by OPPD to Saga constituted part of the gross receipts of Saga's food sales and that such payments were subject to sales tax, affirming the Tax Commissioner's order assessing a deficiency. The Supreme Court reversed, finding instead that the management fees and subsidies were paid for

services rendered (not for the sale of tangible personal property) and as such were not subject to sales tax. In so finding the Court adopted the rationale of an Illinois court finding that such payments were not taxable because "the payments by the employer could not be traced to any specific sale . . . . [and] the evidence showed no basis for relating any portion of the fixed fee or guaranty payment to any individual sale as part of the selling price." *Id.* at 315, 314 N.W.2d at 249 (citing *Chet's Vending Serv. v. Department of Rev.*, 374 N.E.2d 468 (Ill. 1978)).

Unlike the management fees and loss reimbursement payments in *Omaha Public Power District*, *supra*, the Damage Waiver and refueling charges paid by Enterprise customers selecting those options can be traced readily to individual lease transactions. The Court's reasoning in *Omaha Public Power District* indicates that--where charges or fees can be linked to individual sales or lease transactions--those charges should be included in the "gross receipts" from such transactions and subject to sales tax.

The Damage Waiver and Refueling Charges are Part of the Total Consideration Received by Enterprise for Vehicle Rentals and are Not Wholly Separate Transactions

Additionally, the terms of the Lease Agreement under which Enterprise leases or rents vehicles to its customers establish that Damage Waiver charges and refueling charges are part of the total consideration received by Enterprise comprising the lease or rental price of the vehicles and thus are part of the "gross receipts" from the lease or rental price subject to sales tax. Paragraph 3 of the Lease Agreement, titled "Payment by Renter," in subsection (c), states:

> "Renter shall pay Owner . . . (3) [t]he optional equipment, services, and/or product charges . . . . [and] (5) [t]he fuel charge at the rate shown on Page 1. If based on consumption and Vehicle is returned with less fuel than when rented, the charge shall be for the Owner's estimated difference in fuel level shown on the fuel gauge from the time Vehicle is rented to the time it is returned."

(Ex. 4, p.4). The Damage Waiver and refueling charges are listed as part of the Lease Agreement along with other charges that constitute the lease or rental price, such as the daily or weekly charges. "If it is a charge contained in the lease, by clear meaning that is a 'lease charge.'" *Revenue Cabinet v. Budget-Rent-A-Car of Cincinnati, Inc.*, 704 S.W.2d 199, 202 (Ky. 1986) (holding usage tax on the "gross rental or lease charges paid by a customer or lessee renting or leasing a motor vehicle" applied to "*all* charges, including 'total time and mileage,' 'full collision insurance,' 'personal accident insurance,' and 'drop-off charges,' as set out in the lease agreement with Budget as lessor and the customer as lessee."). As such, Damage Waiver and refueling charges included as part of the Lease Agreement are part of the total consideration received by Enterprise for the lease or rental of a vehicle and are included in "gross receipts" as part of the lease or rental price.

Enterprise argues the Damage Waiver and refueling charges should be viewed as completely separate transactions from the lease of the motor vehicle. In response to this argument the Department points to cases from other jurisdictions which have recognized that Damage Waiver and refueling charges imposed by car rental companies are taxable as part of the "gross income," "gross receipts," or "gross proceeds" resulting from the lease or rental of vehicles. For example the court in *City of Phoenix v. Arizona Rent-A-Car Systems, Inc.*, 893 P.2d 75 (Ariz. Ct. App. 1995), found the "refueling charge" assessed when a customer returned a leased vehicle to a car rental company (Budget) without a full gas tank should be included in Budget's taxable "gross income." "Gross income" was defined to include "[t]he total amount of the sale, lease, license for use, or rental price at the time of such sale, rental, lease, or license." *Id.* at 78 n.1. The court rejected Budget's argument that the "refueling charge" was "a separate transaction from the car

rental and not an integral part of it." *Id.* at 78. Rather, the court found that because "[t]he refueling charge is a built-in condition of every Budget car rental contract," "the charge is an integral part of Budget's car rental business," and the "refueling charges paid to Budget are [thus] taxable as gross income from the car rental business." *Id.* at 79–80.

While *City of Phoenix* deals with a privilege tax based on "gross income" as opposed to a sales tax on gross receipts from the lease or rental of tangible personal property, the court finds *City of Phoenix* instructive because the definition of gross income under the Arizona tax statute included the "total amount" of the lease or rental price, and "sale" was defined as "any transfer of title or possession." *Id.* at 78 n.1. These definitions are similar to Nebraska's broad definition of "gross receipts" as the "total amount of the . . . lease or rental price" and the definition of "lease or rental" as "any transfer of possession or control of tangible personal property." NEB. REV. STAT. §§ 77-2701.16(1) and 77-2791.18(1). These definitions, coupled with the definition of "sales price" as "the total amount of consideration . . . for which personal property . . . [is] leased, or rented," demonstrate the similarity between the measure of taxation under Arizona's privilege tax and Nebraska's sales tax. NEB. REV. STAT. § 77-2701.35(1).

In the case of Enterprise's Lease Agreement, refueling charges are part of every contract, although a customer can choose to avoid the refueling charge if the car is returned with a fuel level the same or higher than the fuel level at the time of rental. (Ex. 1, ¶26). The fact that a customer could similarly avoid the refueling charge at issue in *City of Phoenix* did not dissuade the court in that case from finding the refueling charge was an integral part of the lease contract. The same is true under the Lease Agreement between Enterprise and its customers—while the customer may avoid the refueling charge if the car is returned with a fuel level the same or higher

than the fuel level at the time of rental, the refueling charge is still a part of the Lease Agreement and, if assessed, becomes part of the total consideration paid for leasing or renting the vehicle and is included in the lease or rental price. As such, the refueling charges are not a "separate transaction" from the Lease Agreement.

Likewise, the Damage Waiver charges are not separate transactions from the motor vehicle rental transaction, but properly are included in the "gross receipts" subject to sales tax. In *Enterprise Leasing Co. v. Curtis*, 977 So. 2d 975 (La. Ct. App. 2007), the court considered whether "gross proceeds" from the lease or rental of automobiles included any amounts collected by a car rental company (Enterprise) for Damage Waiver payments. Louisiana levies a sales and use tax "upon the lease or rental . . . of tangible personal property" based on "the gross proceeds derived from the lease or rental of tangible personal property." *Id.* at 979. Enterprise claimed Damage Waiver payments were "not part of the 'gross proceeds derived from the lease or rental of tangible personal property'" because they were "a purely optional purchase, separately stated on the face of the rental contract, and thus is a separate purchase and not an integral part of the motor vehicle rental transaction." *Id.*

The court in *Curtis* disagreed with Enterprise's characterization, and held the statute "levying a tax on the 'gross proceeds derived from the lease or rental of tangible personal property' clearly and unambiguously includes [Damage Waiver] payments and shall be applied as written." *Id.* at 981. In reaching its decision, the court looked to the "essence of" or the "real object" of the transaction to determine whether it was taxable. *Id.* at 980. Explaining its conclusion, the court stated:

[T]he real object of the transaction is the lease of tangible personal property, a

> motor vehicle. Clearly, the [Damage Waiver] can only be made available with the lease or rental of a motor vehicle. Enterprise cannot separate the [Damage Waiver] from the principal lease as the [Damage Waiver] does not exist without the automobile lease. Nor can [Damage Waiver] be purchased from another lessor. [Damage Waiver] payments are merely incidental to the lease of the tangible personal property.

Id.

As recognized by the court in *Curtis*, the Damage Waiver charge would not exist without a lease transaction. The Damage Waiver, if elected by the customer, is part of the total consideration paid to lease or rent a vehicle from Enterprise. As the Tax Commissioner in the present case noted, to lease a vehicle from Enterprise the customer must opt to either accept the Damage Waiver and pay a charge, or decline the Damage Waiver and agree to pay for any vehicle damage which occurs during the lease. Similarly, to lease a vehicle from Enterprise the customer must opt either to return the vehicle with the fuel tank filled to the fuel level at the time the vehicle was rented (in which case the customer is obligated to fill the tank prior to returning the vehicle) or opt to pay a refueling charge. In either case, absent the customer's election, no transfer of possession of the vehicle under the lease will occur and, if a customer elects the Damage Waiver and/or refueling charge, those charges are a necessary part of the total consideration paid to lease the vehicle.

An Enterprise customer–while they have options–assumes an obligation regardless of the option chosen. If a customer chooses the Damage Waiver a fee is charged, and if the Damage Waiver is not accepted the customer agrees to pay for damages to the vehicle while it is being leased. Likewise, if the customer agrees to bring the vehicle back with a full tank of gas they will pay for the fuel directly, but if the customer doesn't want to bother filling the tank they agree to pay

a refueling charge to Enterprise. So in either case the "option" a customer has is to pay now or pay later–it is not a choice to be free from the obligation to pay. When an Enterprise customer elects the Damage Waiver or the refueling charge, those charges are part of the total consideration paid to lease the vehicle and properly are considered part of the "gross receipts" from the lease transaction subject to sales tax.

CONCLUSION

After examining the entire record and considering the arguments of the parties, the court finds the Damage Waiver and refueling charges are part of the lease or rental price paid by Enterprise's customers when renting a motor vehicle and properly are included in the "gross receipts" from the lease or rental of motor vehicles subject to Nebraska sales tax.

IT THEREFORE IS ORDERED: The Tax Commissioner's final decision upholding the Department's sales tax deficiency assessment is affirmed in its entirety.

A copy of this order is sent to counsel of record.

DATED this 5th **day of** November**, 2012.**

BY THE COURT:

Stephanie F. Stacy
District Judge