

# Commonwealth Of Kentucky

## Court Of Appeals

NO. 1999-CA-001798-MR

STATE DOCK, INC. and  
POPPLEWELL'S ALLIGATOR DOCK NO., INC.

APPELLANTS

v. APPEAL FROM FRANKLIN CIRCUIT COURT  
HONORABLE ROGER L. CRITTENDEN, JUDGE  
ACTION NO. 97-CI-01543

REVENUE CABINET,  
COMMONWEALTH OF KENTUCKY

APPELLEE

and

NO. 1999-CA-001800-MR

POPPLEWELL'S ALLIGATOR DOCK NO. 1, INC.

APPELLANT

v. APPEAL FROM FRANKLIN CIRCUIT COURT  
HONORABLE ROGER L. CRITTENDEN, JUDGE  
ACTION NO. 98-CI-01578

REVENUE CABINET,  
COMMONWEALTH OF KENTUCKY

APPELLEE

OPINION  
AFFIRMING AS TO 1999-CA-001800-MR

AND

VACATING AND REMANDING AS TO 1999-CA-001798-MR

\*\*\* \*\*

BEFORE: BUCKINGHAM, COMBS, DYCHE, JUDGES.

COMBS, JUDGE: This is an appeal from a Franklin Circuit Court  
judgment affirming a decision of the Kentucky Board of Tax

Appeals that had upheld an assessment of sales and use tax by the Revenue Cabinet against the appellant, Popplewell's Alligator Dock No. 1, Inc. ("Alligator Dock"). The Franklin Circuit Court held that provisions of Kentucky Revised Statutes (KRS) 139.483, exempting specific transactions involving the operation of ships and other vessels from excise taxes, were inapplicable to the appellant's sale of gasoline in association with its lease of houseboats. Consequently, the court agreed with the Revenue Cabinet that the taxes were due and payable. We affirm.

This case was submitted to the Board of Tax Appeals on the basis of stipulations and the deposition of Larry O'Nan, an employee of the Revenue Cabinet. The appellant operates a marina on Lake Cumberland in Russell County, Kentucky. As part of its retail business operation during the period at issue, Alligator Dock leased luxury houseboats to the public -- mostly to vacationers. It collected and remitted sales tax on the rental of the houseboats but did not collect or remit sales and use tax on its sale of gasoline used to power the leased vessels.

Following its audit, a sales and use tax assessment totaling more than Fourteen Thousand Dollars (\$14,000.00) was issued by the Revenue Cabinet.<sup>1</sup> On December 3, 1997, the Kentucky Board of Tax Appeals rendered a decision upholding the Revenue Cabinet's final ruling and assessment of sales and use tax imposed by Chapter 139 of the Kentucky Revised Statutes. The

---

<sup>1</sup>\$2,120.91 of the tax assessment is attributable to sales of gasoline to individuals not renting houseboats from Alligator Dock. Alligator Dock does not question this portion of the assessment and admits that it is correctly due and owed to the Commonwealth.

matter was appealed to the Franklin Circuit Court, which affirmed the decision of the Board of Tax Appeals.

Before the Franklin Circuit Court, Alligator Dock argued that the Revenue Cabinet had erred in failing to conclude that it was entitled to an exemption under the provisions of KRS 139.483. The circuit court disagreed. In its opinion of July 15, 1999, the court focused upon and interpreted two provisions, KRS 139.483 and KRS 139.120. KRS 139.483 provides as follows:

The taxes imposed under the provisions of this chapter [excise taxes on consumption of tangible personal property] shall not apply to the sale of, or the storage, use, or other consumption of, ships and vessels, including property used in the repair or construction of, supplies and fuel consumed in the operation of, and supplies consumed by crew members aboard such ships and vessels which are used principally in the transportation of property or in the conveyance of persons for hire.

KRS 139.120 provides that a "sale" includes the lease of tangible personal property. Since the appellant's lease of a houseboat is to be treated as the "sale" of that vessel under the provisions of KRS 139.120, the court reasoned that the exemption for fuel consumed in its operation is unavailable unless the consumer -- the vacationer -- has engaged the vessel "for hire." Because the vacationers who purchased the gas used to operate the houseboats did not hold or engage the vessels for hire but instead for their own use, the exemption provided by KRS 139.483 was held to be inapplicable. This appeal followed.

There are no facts in dispute in this case. The issue presented, the proper construction of KRS 139.483, is purely a matter of law and is thus subject to de novo review by this

court. Bob Hook Chevrolet Isuzu, Inc. v. Commonwealth, Transportation Cabinet, Ky., 983 S.W.2d 488 (1998). We begin with basic rules of statutory construction: that tax exemptions are to be narrowly construed and that a party seeking an exemption bears the burden of showing that he is entitled to the exemption. Delta Air Lines, Inc. v. Commonwealth, Revenue Cabinet, Ky., 689 S.W.2d 14 (1985); see also KRS 139.260.

The appellant argues that our decision in Barnes v. Department of Revenue, Ky. App., 575 S.W.2d 169 (1978) is dispositive of this appeal. In Barnes, we held that houseboats of a marina operator that were "registered . . . as livery or boats for hire and . . . leased on a weekly basis" were exempt from use tax under KRS 139.483. 575 S.W.2d at 171. We held that the statute has a general application to all ships and vessels which are used primarily in the transportation of property or in the conveyance of persons for hire. Barnes also held that the taxpayer's rental of the houseboats to other persons was a use of those houseboats that constituted a conveyance of persons "for hire" -- thus qualifying for and subject to the exemption. Id.

Despite the superficially factual similarities to Barnes, however, we agree with the Revenue Cabinet with respect to Alligator Dock. The sales and use tax law was significantly altered in 1985 when legislation was enacted to include *bona fide* sales or rentals in the definition of sales or purchases for purposes of the sales and use tax law. This legislative change transformed the incidence or operation of the sales and use tax

statutes generally. As the Revenue Cabinet explains, the sales and use tax statutes do not apply now to the marina operator's initial purchase of the houseboats but instead relate to the subsequent rentals of those houseboats. Thus, the transactions that were at issue in Barnes significantly differ from the case before us, affecting accordingly the issue of whether the KRS 139.483 exemption applies to Alligator Dock's operation. Our inquiry is whether the exemption's requirements are met in the context of the marina operator's rental or leases of houseboats to the vacationers leasing them.

Under the law as enacted in 1985 and applicable here, the exemption provided for by KRS 139.483 does not apply because the lessee's principal use of the houseboat is not the transportation of property or the conveyance of persons for hire. Instead, the lessee's use of the vessel is principally for his personal pleasure or use in the nature of recreation -- a conclusion that is unchallenged and unrefuted by the parties. The present situation is thus indistinguishable from that existing prior to the 1985 amendment where a person purchased (in the pre-1985 sense of the term) a houseboat for his or her personal use and not for rental. Such a transaction clearly would not have been exempt under KRS 139.483 prior to 1985. The only difference between that earlier situation and the present one is that purchases or sales now encompass leases for purposes of the application of the sales and use tax law.

While Alligator Dock agrees that the 1985 statutory amendments authorizing taxation of leases cause the economic

burden of the tax to fall on the lessee, it contends that the tax-exempt status of the property -- the commercial vessel used for "pleasure purposes" -- remains unchanged. Appellant's Brief at 5. Alligator Dock in effect is arguing that commercial houseboats are exempt from sales and use tax -- regardless of their actual use. We disagree in light of the changes brought about by the 1985 amendments, which require us to examine the nature or purpose of the lessee's intended use of the leased vessel.

The fuel used to operate the houseboats in this case was not used in the operation of a ship or vessel principally engaged or used in the transportation of property or the conveyance of persons for hire as required by KRS 139.483. Instead, the gasoline was sold to individuals for use in the operation of houseboats for their personal pleasure or recreational use. We hold that Alligator Dock has not met its burden of showing that the exemption applies to the transaction in question. The trial court did not err by concluding that Alligator Dock's sale of gasoline in this case was subject to taxation.

Alligator Dock also questions the constitutionality of the commercial vessel exemption as applied. We hold that the trial court's interpretation of the exemption does not render the provisions of KRS 139.483 unconstitutional as applied in this case. The Revenue Cabinet's application of the statutory exemption does not discriminate against houseboat taxpayers. Any taxpayer who rents or purchases a houseboat and uses it

principally in the transportation of property or the conveyance of persons for hire is entitled to claim the exemption. Any taxpayer engaged in such transactions for pleasure rather than for hire is not entitled to claim an exemption. The final intended purpose of the use is the determinative factor, and it is neutral in impact and non-discriminatory in application. The judgment of the Franklin Circuit Court, the basis of appeal No. 1999-CA-001800-MR, is thus affirmed.

We now turn to address the sole issue raised by the consolidated appeal: whether taxpayers testing the applicability of KRS 139.483 may proceed directly to court without the necessity of first pursuing and exhausting the administrative procedures of an assessment and appeal to the Kentucky Board of Tax Appeals. On this point, we reverse the trial court's dismissal of the action.

This action was initiated by the filing of a complaint and petition for declaration of rights in the Franklin Circuit Court by State Dock, Inc. ("State Dock"). State Dock requested a declaration that its houseboat leases were exempt from sales and use tax under KRS 139.483 and a permanent injunction preventing the Revenue Cabinet from assessing or collecting sales and use tax for these leases.

Alligator Dock filed an intervening complaint containing similar allegations and seeking similar relief. Later, Alligator Dock amended its complaint to include a claim

that its sales of gasoline in conjunction with the lease of its houseboats were also exempt.<sup>2</sup>

The Revenue Cabinet moved to dismiss the action for lack of jurisdiction. Ultimately, the trial court granted the motion and the action was dismissed. In its opinion and order, the trial court held that the taxpayers were required to pursue the administrative remedies provided by statute before resorting to the courts for relief.

The taxpayers argue that the Revenue Cabinet's imposition of an illegal tax justifies the trial court's use of its equitable jurisdiction to enjoin collection of the tax. They argue that they were entitled to seek a declaratory judgment prior to exhausting their administrative remedies under the case law stated in Gray v. R.J. Reynolds Tobacco Co., 200 Ky. 47, 252 S.W. 134 (1923). R.J. Reynolds Tobacco Co. recognized certain situations where parties are not required to exhaust administrative remedies prior to filing an action in court, including a case in which there is no factual dispute and a party wishes only to ascertain the validity or applicability of a statute or regulation. See also Harrison's Sanitarium, Inc. v. Commonwealth, Ky., 417 S.W.2d 137 (1967) (holding that a party may have direct judicial relief without exhaustion of administrative remedies when there are no disputed factual questions to be resolved and the issue is confined to the validity or application

---

<sup>2</sup>As related above, Alligator Dock also raised this issue in proceedings before the Kentucky Board of Tax Appeals. The matter before the Board of Tax Appeals culminated in the appeal resolved above; it was consolidated by our order entered September 22, 1999, with the appeal now under discussion.

of a statute or ordinance or administrative regulation); Franklin v. Natural Resources and Environmental Protection Cabinet, Ky., 799 S.W.2d 1 (1990).

The taxpayers have conceded that in the event that the exemption be construed to be unavailable to them, the tax is due and owing. There are no factual questions to be resolved; a single legal question remains: the proper construction and application of KRS 139.483. The taxpayers' protest falls squarely within the exception to the general rule requiring the exhaustion of administrative remedies.

Because the trial court improperly declined jurisdiction in this separate but related matter, we remand this action (appeal No. 1999-CA-001798-MR) for further proceedings consistent with the entirety of this opinion.

ALL CONCUR.

BRIEF AND ORAL ARGUMENT FOR  
APPELLANTS STATE DOCK, INC.  
AND POPPLEWELL'S ALLIGATOR  
DOCK NO.1, INC.:

Leslie Rosenbaum  
Lexington, KY

BRIEF AND ORAL ARGUMENT FOR  
APPELLEE REVENUE CABINET:

Douglas M. Dowell  
Frankfort, KY