IN THE SUPERIOR COURT OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

PROFESSIONAL STAFF LEASING CORPORATION, and MELMER CORPORATION, Appellants,	:	
v.	:	C.A. No. 04A-09-008 SCD
DIRECTOR OF REVENUE, Appellee.	:	

Submitted: June 1, 2005
Decided: July 7, 2005

OPINION

This appeal from a decision of the Tax Appeal Board challenges the application of the gross receipts statute. Taxpayer provides services to clients which include the payment of State and Federal taxes. The Director has ruled that the monies which pass through taxpayer's account are subject to the tax because they are part of the total consideration received. I affirm the Board's ruling.

Facts

Appellant, Professional Staff Leasing Corporation ("ProLease")[1] is a professional employer or "PEO." The parties have stipulated to the following. "A PEO contractually assumes substantial employer rights, responsibilities and liabilities through the establishment and maintenance of an employer relationship with the client's workers. ProLease's activities as a PEO include providing payroll services, benefits administration,

[1] Two matters were consolidated before the Tax Appeal Board. One involved ProLease, and the other was ProLease's successor corporation, Melmer Corporation. The ruling below was as to both corporation, as is this ruling.

and human resources advice/consulting. ProLease does not supply its clients with temporary or permanent employees, rather ProLease co-employs the employees that ProLease's clients already have working for them (such employees shall be referred to herein as the "worksite employees").”[2]

The Court has been provided with two contracts governing the relationship between ProLease and its client. The first one is dated 2000, the second one is dated 2001. The 2001 contract contains an automatic renewal provision. Each contract states clearly that ProLease is to be a co-employer with the client.[3] The parties have stipulated that "ProLease's payment of federal and state withholding taxes and federal unemployment taxes are made under its own federal employer identification number, not the federal employer identification number of its clients.”[4]

The parties agree that ProLease is properly licensed as a general service provider under 30 *Del. C.*§ 2301(b). Delaware's gross receipts tax for general service provider is

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[2] Statement of Stipulated Facts, paragraph 2.

[3] The 2000 contract provides:

By this agreement, ProLease agrees to assume certain of Clients' Common Law Employer responsibilities and liabilities. ProLease further agrees to hold Client harmless, subject to the terms of this Agreement, with respect to all such responsibilities and liabilities assumed. In that regard, ProLease and Client shall act as **joint co-employers** with respect to the employees of Client. . . . ProLease is specifically responsible for payment of employee payroll, employer federal, state and local taxes, specified employee benefits, and all required federal, state and local employee payments or withholdings from wages. All benefits will be provided and all taxes will be paid under **ProLease's federal and state tax identification numbers**. (Emphasis supplied) Client Service Agreement, paragraph 2. Services.

The 2001 contract provides:

ProLease shall provide client with professional employer services including payroll, ... ProLease and the Client shall be co-employers of the worksite employees (“Employees”), both having an employment relationship with the Employees hereunder. As a co-employer, ProLease shall have the authority and right to direct, control, hire, terminate or supervise all Employees pursuant to this Agreement. Client Service Agreement, paragraph 1. Relationship.

* * * * *

As a co-employer, the Client shall retain the authority and right to direct, control, supervise, hire, discipline and discharge the employees. The Client shall specifically have the sole right to direct and control Employees in the manufacturing, production, and/or delivery of Clients products and services. The Client shall provide Employees with tools, instrumentalities and a place of work. Id. at 5.A.

[4] Statement of Stipulated Facts, paragraph 6.

found at 30 *Del.C.* § 2301(d)(1) which provides in pertinent part that "[E]very person shall also pay a license fee at the rate of 0.384% of the aggregate gross receipts paid to such person attributable to activities licensable under this chapter . . . .."

"Gross receipts" is defined as the "total consideration for services rendered, goods sold, or other-income producing transaction within this State, including fees and commissions."[5]

The Director of Revenue ("Director") issued ProLease a gross receipts tax assessment for the calendar year 2001 in the amount of $26,817.42. The Director's tax assessment was based upon the total amount of payments received by ProLease from its client, rather than upon the administration fee paid to ProLease by its client. ProLease appealed the Director's decision to the Tax Appeal Board. The Board affirmed the Director, concluding that "the compensation [ProLease] receive[s] from their clients, including the funds which [ProLease] receive[s] in the form of employee gross wages, federal and state taxes, workers' compensation premiums, and employee benefit deductions" meet[s] the definition of Gross Receipts.[6] A timely appeal was filed.

The issue on a appeal is whether ProLease is required to include in its gross receipts the money which it receives from its client, and passes through its accounts to pay the various state and federal taxes and other financial obligations due from client, and assumed by ProLease pursuant to its contract, or whether the gross receipts tax should be calculated on the basis of its service fee only.

[5] 30 *Del. C.* § 2301(e)
[6] Decision and Order of the Tax Appeal Board, August 13, 2004.

Standard of Review

In reviewing a decision of the Board, this Court must take due account of the experience and specialized competence of the Board, and of the purposes of the basic law under which the Board has acted. This Court's review is limited to a determination of whether the agency's decision was supported by substantial evidence and correct as a matter of law.[7]

Analysis

The ruling below was based on two prior decisions of the Superior Court, each relying on language in 30 *Del. C.* 2120(a). *Atlantic Richfield Company v. Director of Revenue*[8] considered the issue of whether a gasoline wholesaler, selling in Delaware, was required to include in the calculation of its gross receipts tax the federal and state gasoline taxes it was obliged to pay as a seller of gasoline. Atlantic argued that the federal and state gasoline taxes were not a part of the consideration it receives from the sale of gasoline. Thus, the taxes should not be included in gross receipts. Relying on specific statutory language expressly prohibiting a deduction for federal or state taxes,[9] the Superior Court held that such taxes were includable in the calculation, just as the cost of a tobacco product tax stamp would be included in the computation of gross receipts in the sale of cigarettes.[10]

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[7] Administrative Procedures Act, 29 *Del. C.* § 10142(d); *United Water Delaware, Inc. v. Public Service Com'n*, Del. Supr., 723 A.2d 1172, 1173 (1999).
[8] 346 A.2d 184 (Del. Super. 1975)
[9] Section 2120(a) provides: Wherever this Part [referring to the licensing part applicable to the taxpayer] uses the term "gross receipts," no deduction shall be made therefrom on account of the cost of property sold, the cost of materials used, labor costs, interest, discount paid, delivery costs, federal or state taxes or any other expense whatsoever paid or accrued or losses, ..."
[10] 346 A.2d at 186.

The second case relied upon below is *Director of Revenue v. Gove*.[11] *Gove* considered the issue of whether a self-employed carpenter who did small home improvements jobs on a time and materials basis must include the cost of the materials in calculating his gross receipts. On appeal, the Superior Court ruled that since the Code specifically defines gross receipts to including "the cost of the materials used"[12] the cost of the carpenter's materials were includable in its gross receipts.[13]

ProLease distinguishes *Gove* by arguing that ProLease is an agent of its client and the client is liable for the payment of the employee's wage. ProLease distinguishes *Atlantic Richfield* on the grounds that the gasoline customers did not have the obligation to pay the taxes, only the taxpayer did, and that made the taxes an expense of the business—not excludable for gross receipt purposes.

The question of whether or not a taxpayer is required to include in its gross receipts calculation the monies which are paid on behalf of a client turns on the nature of the relationship between the taxpayer and the client. If the taxpayer is an agent for the client, typically, the monies or properties are not includable. Conversely, if the taxpayer is an employer, the monies are included. A discussion of two of the cases cited by the parties demonstrates the point.

Brim Healthcare, Inc. v State of New Mexico[14] considered an assessment of gross receipts tax on a taxpayer who received fees for staffing hospitals with management personnel. The court determined that reimbursement for salaries and benefits paid to employees working at hospitals were subject to the tax. The Court noted that Brim was

[11] *Director of Revenue v. Gove*, 1985 WL 549244 (Del. Super).
[12] *Supra* at 7.
[13] *Gove*, 1985 WL 549244 at *2.
[14] 896 P.2d 498 (N. M. Ct. App. 1995).

acting at all times as an independent contractor in performing its services, not as an agent of the hospitals. The personnel remained Brim employees and Brim was expending the reimbursed monies *to meet its own responsibilities*.[15]

Aabakus, Inc. v Huddleston[16] involves a taxpayer which performed services for its clients much like those provided by ProLease in the case at bar. The taxpayer was a "rentable human resources department'[17] providing services which were much more than simple accounting auditing and bookkeeping services. The court described the taxpayer as the employer "on paper,"[18] but noted that the employees remained under the direct control and supervision of the client.

The court in *Aabakus* discounted the status of the taxpayer as employer. It concluded that the client was the employer-in-fact, notwithstanding evidence that Aabakus represented itself as the employer to the Tennessee Department of Employment Security. Applying a statute which included in the definition of sales price for tax purposes "the total amount for which . . . services rendered is sold . . . without any deduction there from on account of the . . . labor or service cost . . . or any other expense whatsoever", the Court concluded that the only amount taxable was the amount which remained after the clients' third-party payments were made.

Brim is on point. The facts of this case show that ProLease assumed the legal status of co-employer, and by doing so, obligated *itself* to pay the requisite salaries, taxes and benefits.

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[15] *Id.* at 500.
[16] *Aabakus, Incorporated v. Huddleston*, 1996 WS 548148 (Tenn. Ct. App.)
[17] *Id* at p. 3
[18] There is no elaboration in the opinion explaining the source of the reference to an "employer on paper" although I surmise that it means something written in the contract between the taxpayer and client.

Aabakus supports ProLease's position. I do not find the reasoning to be persuasive because there is a factual distinction, ProLease is a co-employer. The money passing through its accounts discharges its own contractually assumed liability. It holds itself out to the federal government as an employer by using its own federal employer identification number to execute the filings. Those circumstances make it more than an agent, it is a principle.

Conclusion

The issue below was presented to the Board on stipulated facts. There is no factual error in the decision of the Board, nor is there an error of law.

The decision below is AFFIRMED.

IT IS SO ORDERED.

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Judge Susan C. Del Pesco

Original to Prothonotary
xc: Leonard S. Togman, Esquire
John J. Quinn, III, Esquire
Joseph Patrick Hurley, Jr., Esquire
Tax Appeal Board