

Chapter 2. Sales Tax

Oil and gas companies are subject to state taxation on their purchases and sales of goods and services. Louisiana has a number of tax provisions that either directly or indirectly affect the oil and gas industry. Oil and gas companies should be aware of these tax provisions and their opportunities for structuring transactions to take advantage of tax exemptions and exclusions.

I. Introduction to Sales and Use Taxation

In the United States, sales tax is most commonly imposed at the state and local level. Unlike an income tax or property tax, the sales tax is an “indirect tax,” which means the burden of collecting the tax falls on the seller—or the buyer—rather than being collected directly by the taxing authority. The sales tax is also considered a “regressive tax,” because everyone pays the same amount of tax, without reference to wealth or income.

Where it is imposed, sales tax typically includes a complementary use tax provision. The sales tax is imposed on purchases made in the state imposing the tax. Prior to the imposition of a use tax, differences in sales tax rates and states that did not impose a sales tax allowed purchasers to forum shop, seeking out low or no tax jurisdictions. As a result, states imposed a use tax, which taxes the use, storage or consumption of property in the state.

[A] ‘use’ tax is an integrated part of a sales tax, its purpose being to remove the buyers' temptation to place their orders in other states in the effort to escape payment of the tax on local sales. In view of this declaration it would seem that the ‘use’ tax provided for in LRS 47:301 et seq. was primarily intended to affect items purchased out of this state for immediate importation to and use in this state—a tax in lieu of the sales tax.¹

To prevent double taxation, purchasers are allowed to lower the use tax owed to Louisiana by the amount of sales or use tax paid to another state or local taxing authority.²

The Louisiana sales tax is a consumer tax, with the measure of the tax based on the sales price of the good or service.³ Specifically, Louisiana taxes “the sale at retail of each item or

¹ *Fontenot v. S. E. W. Oil Corp.*, 232 La. 1011, 1017, 95 So.2d 638, 640 (1957).

² *Word of Life Christian Ctr. v. W.*, 2004-1484 (La. 4/17/06); 936 So.2d 1226, 1234.

³ A sales tax is a single-stage tax on consumer spending that applies to final sales for personal use and consumption. *Word of Life Christian Ctr. v. W.*, 2004-1484 (La. 4/17/06); 936 So.2d 1226, 1233.

article of tangible personal property.”⁴ Therefore, sellers must identify if they are making a sale. Louisiana defines “sale” to include a broad range of transactions: “any transfer of title or possession, or both, of tangible personal property, for a consideration, and includes the furnishing, preparing, or serving, for a consideration, of any tangible personal property, consumed on the premises of the person furnishing, preparing, or serving such tangible personal property.”⁵ However, Louisiana does not impose a tax on “occasional sales.”⁶ Consequently, “an isolated sale by a person not engaged in the business of selling” will not be subject to sales tax.⁷ “Business” includes any activity engaged in for “gain, benefit, or advantage.”⁸

II. Is it a Sale of Tangible Personal Property or a Sale of Services?

A large portion of sales tax litigation focuses on whether the item being sold qualifies as tangible personal property or a nontaxable sale of services. The controversy is a result of the divergent tax treatment of goods and services.

For the sale of goods, states—including Louisiana—tax all retail sales, unless explicitly exempted.

There is hereby levied **a tax upon** the sale at retail, the use, the consumption, the distribution, and the storage for use or consumption in this state, of **each item or article of tangible personal property**, as defined herein, the levy of said tax to be as follows:

(1) [Sales Tax] At the rate of two per centum (2%) of the sales price of each item or article of tangible personal property **when sold at retail** in this state; the tax to be computed on gross sales for the purpose of remitting the amount of tax due the state, and to include each and every retail sale.

(2) [Use Tax] At the rate of two per centum (2%) of the cost price of each item or article of tangible personal property when the same is not sold but is **used**,

⁴ LSA-R.S. 47:302(A).

⁵ LSA-R.S. 47:301(12).

⁶ LSA-R.S. 47:301(10)(bb).

⁷ Id.

⁸ LSA-R.S. 47:301(1). The term “business” does not “include occasional and isolated sales by a person who does not hold himself out as engaged in business.” LSA-R.S. 47:301(1).

consumed, distributed, or stored for use or consumption in this state; provided there shall be no duplication of the tax.⁹

The Louisiana Department of Revenue has confirmed the status as tangible personal property—and therefore taxable property—of a number of items relevant to the oil and gas industry. Ships, vessels, barges and boats of whatever size constitute tangible personal property. The “proppant” or sand used in providing hydraulic fracturing services is also considered taxable tangible personal property.¹⁰

Although the sales tax is imposed on the sale of services as well as the sale of goods, only explicitly enumerated services are subject to sales taxation. Louisiana's sales and use tax law defines “sales of service” in Section 301(14). One of those specifically enumerated taxable services is the repair of tangible personal property.¹¹

Louisiana’s defined taxable services leave the provision of a number of oil and gas related services as nontaxable sales. The completion of new oil and gas wells, reworking existing wells, and hydraulic fracturing are not taxable services in Louisiana.¹² Because, in Louisiana, oil and gas wells, as well as drilling platforms mounted on the ocean floor, are treated as immovable property,¹³ the sale of services repairing oil and gas wells is not subject to sales tax.¹⁴ Reworking and fracturing are also considered nontaxable repair services.¹⁵ Moreover, Louisiana law also explains that the repair, renovation or conversion of a drilling rig, or its component parts, used exclusively for exploration or development of minerals outside state territorial limits is not a taxable service.¹⁶

III. Sales Tax Exemptions, Exclusions and Other Nontaxable Sales

The application of exemptions from sales and use taxation is another major source of controversy in sales tax. The purpose of a general retail sales tax is to tax the final sale of a product and tax it only once. In the words of the Louisiana Supreme Court, “[s]ales and use taxes are consumption taxes, meaning they are intended to apply to the final stage in the sales

⁹ LSA-R.S. 47:302(A).

¹⁰ Sales Tax: Oil & Gas Well Fracturing Services, Rev. Ruling No. 10-003 (Nov. 10, 2003).

¹¹ LSA-R.S. 47:301(14)(g).

¹² Rev. Ruling No. 10-003.

¹³ LSA-R.S. 47:301(16)(l).

¹⁴ Rev. Ruling No. 10-003.

¹⁵ *Id.*

¹⁶ LSA-R.S. 47:301(14)(iii).

transaction imposed on specific sales.”¹⁷ Consequently, states do not tax sales made to buyers intending to resell. Resale often includes re-leasing or re-renting.¹⁸

Similarly, states often exclude from taxation the sale of component parts destined to become part of a larger good for sale. Other exemptions also have their foundation in the theory that products should only be taxed only once, including, for example, the exclusion from tax of sales of machinery or equipment that will be used to make an item destined for later sale.

By nature, the field of sales taxation is finicky and detail oriented. Louisiana has various exclusions specific to the oil and gas industry. The following are exempted or excluded from sales and use taxation:

- ◆ Separately stated charges to install board roads for oilfield operators;¹⁹
- ◆ For drilling rigs used exclusively for the exploration or development of minerals in federal offshore areas, the labor, materials, services and supplies used for the repair, renovation, or conversion of any drilling rig or machinery and equipment which become component parts of the drilling rig;²⁰
- ◆ “Sales of materials, equipment, and machinery which enter into and become component parts of . . . drilling ships, or drilling barges, of fifty tons load displacement and over, built in Louisiana [and] the gross proceeds from the sale of such ships, vessels, or barges when sold by the builder thereof;”²¹ and
- ◆ The lease or rental entered into for the purpose of re-lease or re-rental of casing, tools, pipe, drill pipe, tubing, etc., used in connection with the operating, drilling, completion, or reworking of oil, gas, sulphur, or other mineral wells.²²

¹⁷ *Word of Life Christian Ctr. v. W.*, 2004-1484 (La. 4/17/06); 936 So.2d 1226, 1232.

¹⁸ LSA-R.S. 47:301(7)(b) (“The term ‘lease or rental’, however, as herein defined, shall not mean or include the lease or rental made for the purposes of re-lease or re-rental of casing tools and pipe, drill pipe, tubing, compressors, tanks, pumps, power units, other drilling or related equipment used in connection with the operating, drilling, completion, or reworking of oil, gas, sulphur, or other mineral wells.”).

¹⁹ LSA-R.S. 47:301(3)(c).

²⁰ LSA-R.S. 47:301(14)(g)(iii).

²¹ LSA-R.S. 47:305.1(A); *see also* Sales & Use Tax: Taxability of Purchases for Maritime Transportation Vessels, Drilling Barges, and Drilling Ships, Rev. Ruling No. 06-015 (Sept. 19, 2006).

²² LSA-R.S. 47:301(7)(B)

Moreover, oil and gas case law provides a number of illustrations of the detailed and persnickety factual investigations required for much of sales tax litigation:

- ◆ Cleaning oil field drilling tubing is not subject to parish sales tax as either a cleaning service or repairs to tangible personal property.²³
- ◆ No sales or use tax is paid for coke-on-catalyst.²⁴
- ◆ Gas consumed by Company for purposes of fueling Company's compression unit is protected from taxation by La. Const. art. 7, § 4(B) and is valueless for sales and use tax purposes.²⁵
- ◆ Gas consumed by Company for purposes of fueling Company's compression unit was acquired through a "taxable barter," and imposing sales tax on customer supplied gas does not violate La. Const. art. 7.²⁶
- ◆ The transfers of its gas by the customers to Company to power Company's compression unit constituted a sale, because it constituted the transfer of title or possession of tangible personal property for "a consideration," as required under by the Louisiana sales tax statute.²⁷

IV. Conclusion

Oil and gas companies should be aware of sales and use tax provisions and the opportunities available to structure transactions advantageously. Louisiana has a number of tax

²³ *Intracoastal Pipe Serv., Co., Inc. v. Assumption Parish Sales & Use Tax Dep't*, 558 So.2d 1296, 1300 (La. Ct. App.1990) writ granted in part, denied in part, 563 So.2d 863 (La.1990). However, cleaning, redoping, sandblasting, waterblasting, and internal and external brushing and spraying of oil filed drill pipe are subject to Louisiana sales and use tax under LSA-R.S. 47:301(14)(g) as services on tangible personal property.

²⁴ *State v. Star Enter.*, 95-2124 (La.App. 4 Cir. 8/7/96); 691 So.2d 1221, 1228 writ granted, 96-2218 (La. 9/19/96); 679 So.2d 409 and *aff'd sub nom.* *State v. BP Exploration & Oil, Inc.*, 96-0716 (La. 1/14/97); 686 So.2d 823 (Coke-on-catalyst is subject to use tax, but there is no tax due because it lacks market value and has no actual cost); see also *Sch. Bd. of Parish of St. Charles v. Shell Oil Co.*, 435 F.Supp.2d 531, 539 (E.D. La.2006) (citing La. Const. art. 6, sect. 28) ("[C]oke-on-catalyst is specifically mentioned as a tax-exempt by-product in La. R.S. § 47:301(18)(d)(ii), and . . . coke-on-catalyst used for boiler fuel falls under the boiler fuel exemption. Therefore, coke-on-catalyst is exempt from taxation except to the extent that active authorized bonds were secured by taxes at the time the exemptions were passed.").

²⁵ *Hanover Compressor Co. v. Dep't of Revenue*, 2002-0925 (La.App. 3 Cir. 2/5/03); 838 So.2d 876, 883.

²⁶ *Bridges v. Prod. Operators, Inc.*, 2007-0648 (La.App. 4 Cir. 12/12/07); 974 So.2d 54, 62.

²⁷ *Columbia Gulf Transmission Co. v. Bridges*, 2008-1006 (La.App. 1 Cir. 6/25/09); 28 So.3d 1032, 1042-43 writ denied, 2010-0116 (La. 4/5/10); 31 So.3d 371 and writ denied, 2010-0249 (La. 4/5/10); 31 So.3d 369.

provisions that either directly or indirectly affect the oil and gas industry. And, the oil and gas industry has been both directly and indirectly subjected to and exempted from state and local taxation on purchases and sales of goods and services.