

This decision was appealed to the Iowa District Court and affirmed by the Iowa District Court Iowa State Association of Counties vs Iowa Department of Revenue, CVCV063262.

Iowa Department of Inspections and Appeals
Division of Administrative Hearings
Wallace State Office Building
Des Moines, Iowa 50319

IOWA STATE ASSOCIATION
OF COUNTIES

Case No. 20IDR0044
Rev. Nos. 2012-300-1-0344,
2014-300-1-0282

Appellant,

vs.

PROPOSED DECISION

IOWA DEPARTMENT OF
REVENUE

Respondent.

STATEMENT OF THE CASE

The Iowa State Association of Counties ("ISAC") filed an appeal from the decision of the Department of Revenue ("Department") denying its request for a refund of sales tax paid during the 2010 through 2014 tax years. This matter came on for hearing at the Wallace State Office Building on June 3, 2021. Attorneys Dwayne Vande Krol and Thomas Goodhue appeared on behalf of ISAC. Also present on behalf of ISAC was Kristi Harshbarger, Grant Hyland, and Wes Greder. Assistant Attorneys General Katherine Penland and Adam Humes represented the Department.

The record includes ISAC's exhibits 1 through 21 and the Department's exhibits A through Z and AA through AT. The record additionally includes the testimony of the following individuals: William Peterson, Darin Raymond, Grant Veeder, Burlin Matthews, Rhonda Deters, Dewey Hildebrant, Carla Becker, Brad Holten, and Steve Campbell.

ISSUE

Whether the Department properly denied ISAC's request for a refund of overpaid sales tax from 2010 through 2014.

FINDINGS OF FACT

ISAC originated from an association of multiple county officials through the state, and was organized in 1964 under the Iowa Non-Profit Corporation Act found in Chapter 504 of the Iowa Code. Per ISAC's Articles of Incorporation, its purposes are to

maintain a permanent organization to secure cooperation among the several counties of the State of Iowa and the public officers of the several counties in a

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comprehensive study of local problems and in the application of knowledge obtained to procure efficient methods of local government; to provide ways and means whereby the county officials of the several counties of this state may interchange ideas and experiences and obtain expert advice; to so organize and coordinate activities between the several counties as to be able to advise and cooperate with the Iowa General Assembly and the Congress toward the enactment of legislation that will be of most benefit to the citizens of the state; to do any and all other things necessary, proper or fitting to carry out the objects herein expressed or for the benefit of the counties or county officials of the State of Iowa and to engage in any and all lawful activities for which corporations may be organized under the Iowa Non-Profit Corporation Act.

In short, ISAC was created to "perpetuate and strengthen county government and to facilitate the exchange among county officials." (ISAC's Exhibit 1; State's Exhibits K, L; Peterson Testimony).

Iowa counties themselves are eligible for membership to ISAC; however, they are eligible for general membership-only. General members have no voting rights, other than for questions presented at annual or special meetings of corporation. Additionally, elected county officers or county employees may become members. Per its bylaws, the entire control of ISAC, its affairs, and property is vested in its Board of Directors. The members of its Board of Directors are seated and certified by the following affiliate associations:

Iowa State Association of County Supervisors; Iowa State Sheriffs' and Deputies' Association; Iowa County Attorneys Association, Inc.; Iowa State Association of County Auditors; Iowa State County Treasurers Association; Iowa County Recorders Association, Inc.; Iowa County Engineers Association; Iowa State Association of Assessors; Iowa Community Services Association; Iowa Emergency Management Association; County Conservation Directors Association of Iowa; Iowa Director, National Association of Counties; Iowa Environmental Health Association, Inc.; Iowa Counties Public Health Association; County Zoning Officials of Iowa; Iowa Counties Information Technology Organization; and the immediate past three presidents of ISAC.

The Executive Director of ISAC is a member ex officio of the Board of Directors. The Board of Directors has exclusive authority to hire, fire, and supervise ISAC's Executive Director. The Executive Director, in turn, manages the organization's day-to-day operations. (ISAC's Exhibits 1, 2, 21; Peterson Testimony).

Further, per ISAC's bylaws, its listed affiliated associations have the power to conduct schools of instruction, conferences, or meetings. The affiliated associations also determine their own memberships; however, only county officers, county employees and employees of conference boards are eligible to become voting members of each respective association. (ISAC's Exhibit 2).

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At all times relevant herein, all 99 counties annually paid membership dues. The remainder of ISAC's annual operating budget is funded by a combination of other membership dues, insurance premiums, sponsorships, advertising, and the sale of services and programs to its members. (W. Peterson Testimony; State's Exhibit L; ISAC's Exhibit 20).

ISAC offers many programs and services to its members. It provides lobbying services to promote legislation for the benefit of its members. ISAC holds regular conferences for the purposes to providing educational and networking opportunities for those involved in county government. It provides training, education and support for issues important to county governments, such as legal compliance, human resources, and information technology. Several county officials and employees attend ISAC training as part of their official office or employment. ISAC's members find the programming to be very useful, and if the organization had not offered them, they would be tasked with finding similar offerings elsewhere. (State's Exhibits L, N, O, P, Q, R, AE; ISAC's Exhibits 3, 4, 5, 6, 7, 8, 9, 11, 15; Peterson Testimony; Hildebrandt Testimony; Veeder Testimony; Matthews Testimony; Deters Testimony; Becker Testimony).

ISAC also sponsors and manages a number of insurance programs for its member counties. It operates three self-funded insurance pools: for health insurance, voluntary accidental death and dismemberment insurance, property and casualty insurance, and unemployment insurance. Additionally, ISAC provides services related to the compliance of the Health Insurance Portability and Accountability Act of 1996 (HIPAA) and case management and mental health disability services (CMDs) through an agreement with counties pursuant to Iowa Code chapter 28E.¹ (State's Exhibits L, N, O, P, Q, R, AE; Peterson Testimony; Hildebrandt Testimony; Veeder Testimony; Matthews Testimony; Deters Testimony; Becker Testimony; ISAC's Exhibits 3, 4, 5, 6, 7, 8, 9, 11, 15).

Moreover, ISAC maintains listings of preferred commercial enterprises, professional organizations, or private groups who may be of interest to its membership. Those preferred organizations pay a fee to be associated with ISAC. In addition, ISAC participates in activities such as publishing an informational magazine and website for its membership, which includes the sale of advertisements. ISAC also manages a scholarship fund for eligible children of participating county employees. (State's Exhibits L, N, O, P, Q, R, AE; Peterson Testimony; Hildebrandt Testimony; Veeder Testimony; Matthews Testimony; Deters Testimony; Becker Testimony; ISAC's Exhibits 3, 4, 5, 6, 7, 8, 9, 11, 15).

ISAC filed a petition for a declaratory order with the director of the Department on December 29, 2010 to decide whether it was exempt from paying sales and use tax as an instrumentality of government pursuant to Iowa Code section 423.3(31). In its February 17, 2011 declaratory order, the Department concluded counties lacked sufficient control of ISAC for it to be considered a government instrumentality. ISAC initially petitioned for judicial review of the decision, but later voluntarily dismissed the action. (State's Exhibit A).

¹ See I.C.A. 28E.1 (stating the purpose of the chapter is "to permit state and local governments in Iowa to make efficient use of their powers by enabling them to provide joint services and facilities with other agencies and to cooperate in other ways of mutual advantage.").

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ISAC later filed another petition for a declaratory order on February 20, 2012, again asking the director of the Department to decide whether it was exempt from paying sales and use tax as an instrumentality of government pursuant to Iowa Code section 423.3(31). In response, the director declined to issue an order, stating:

Whether the Petitioner is exempt from paying sales and use tax under Iowa Code § 423.3(31) as an instrumentality of the county government is a highly factual question. Due to the highly factual nature of the issue presented in the Petitioner's request and the need for additional information by the Department to adequately address the issue involved, it is the Director's opinion that the issue presented would more properly be resolved through the refund claim process, during which the Department and Petitioner can informally discuss the issue, obtain more facts, and fully explore the affidavits and other documents referenced in the Petition.

(Director Decision Feb. 20, 2012).

ISAC then filed Iowa Form 843 Claim for Refund for the sales and use taxes paid by the organization from the fourth quarter of 2010 through the first quarter of 2014. ISAC's cited reason for the request was that it was exempted as an instrumentality of county governments and thus overpaid sales and use tax during that time. The Department subsequently denied the refund requests in written decisions dated August 15, 2012 and August 6, 2014, concluding ISAC is not eligible for the exemption. ISAC timely protested the Department's decisions. (State's Exhibits C-F; Protests).

CONCLUSIONS OF LAW AND ANALYSIS

The Department's Director administers the assessment and tax laws in Iowa.² The Iowa Legislature has granted the Department's Director the express authority to adopt rules "for the orderly and methodical performance" of the Director's duties.³

As an initial matter, the Department has argued both in its motion for summary and post-hearing brief that the Director of the Department's declaratory order issued February 17, 2011 is binding and controlling in this case. The undersigned administrative law judge already considered the argument in her ruling denying the Department's motion for summary judgment filed in this case, and declines to revisit it in this decision.

Iowa Code section 423.2 imposes a sales tax upon several enumerated goods and services. Iowa Code section 423.3 provides for a number of exemptions from sales tax. The sole issue in this case is whether the Department properly denied ISAC's request for a refund of overpaid sales tax from 2010 through 2014. The burden of proof is upon ISAC to show that the request for a refund was improperly denied.⁴

² Iowa Code § 421.17.

³ Iowa Code § 421.14.

⁴ Iowa Code § 421.60(6)(c).

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ISAC argued it is entitled to a refund for sales taxes paid those years because it is exempted as a government instrumentality pursuant to Iowa Code section 423.3(31). That provision exempts an entity from the provisions of Iowa Code chapter 423 (Sales Tax) and from the computation of the amount of tax imposed by it in the following ways:

...all divisions, boards, commissions, agencies, or instrumentalities of state, federal, county, municipal, or tribal government which have no earnings going to the benefit of an equity investor or stockholder, except any of the following:

- a. The sales price of tangible personal property or specified digital products sold to, or of services furnished, and used by or in connection with the operation of any municipally owned public utility engaged in selling gas, electricity, heat, pay television service, or communication service to the general public
- b. The sales price of furnishing of sewage services to a county or municipality on behalf of nonresidential commercial operations.
- c. The furnishing of solid waste collection and disposal service to a county or municipality on behalf of nonresidential commercial operations located within the county or municipality.

The party claiming an exemption bears the burden of proving entitlement to it.⁵ Tax exemption statutes are narrowly construed in favor of taxation.⁶

The phrase “instrumentalities of ...government” is not specifically defined by the statute at issue for this case. When a term is not defined by statute or interpreted in the associated regulations, the words are assigned their common, ordinary meaning, in the context of the statute and its history.⁷ Courts also “construe statutes harmoniously with other statutes related to the same subject matter or to closely allied subjects.”⁸ One must interpret a term in a manner consistent with the statute as an integrated whole.⁹

The problem in this case is that “instrumentality of government” is not clearly defined. Legal precedent or statutory guidance is sparse. Our state’s Supreme Court has described a substantially similar concept, “federal instrumentality,” as having a “chameleon-like character,” making it difficult to specifically define and identify.¹⁰

The parties agree there are two prevailing mechanisms to determine whether a private organization is an instrumentality of government. The parties, however, do not agree how to apply those mechanisms in this case. The first mechanism, commonly referred to as the “control

⁵ *Iowa Ag. Constr. Co. vs. Iowa State Bd. Of Tax Review*, 723 N.W.2d 167, 174 (Iowa 2006); *Katridg Pak Co. vs. Dept. of Revenue*, 362 N.W.2d 557, 561 (Iowa 1985).

⁶ *Iowa Ag. Constr. Co.*, 723 N.W.2d at 174; see also *Dial Corp. v. Iowa Dept. of Revenue*, 634 N.W.2d 643, 646 (Iowa 2001) (“Tax exemption statutes are construed strictly, with all doubts resolved in favor of taxation.”).

⁷ *Myria Holdings, Inc. & Subs vs. Iowa Dept. of Rev.*, 892 N.W.2d 343, 348 (Iowa 2017).

⁸ *Id.* (citations omitted).

⁹ See *Cohwell v. Iowa Dept. of Human Services*, 923 N.W.2d 225, 233 (Iowa 2019) (defining term “individual” after reviewed how the term was used elsewhere in same chapter).

¹⁰ *South Central Iowa Production Credit Ass’n vs. Scanlan*, 380 N.W.2d 699, 701 (Iowa 1986).

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test” pursuant to *United States vs. Orleans*, considers whether the governmental body which the entity claims it is acting on behalf of has the right to control the “detailed physical performance” of the entity.¹¹ In applying the control test, the overall question is whether the governmental body supervises the entity’s daily operations.¹²

The other method utilized is the *Wachovia* test as set forth by the North Carolina Supreme Court in *Unemployment Compensation Commission of North Carolina vs. Wachovia Bank & Trust Co.*, 2 S.E.2d 592 (North Carolina 1939).¹³ This test looks at the following factors:

1) whether the organization was created by the government; 2) whether the organization is wholly owned by the government; 3) whether the organization is operated for profit; 4) whether the organization is primarily engaged in the performance of some essential government function; and 5) whether the proposed tax would impose an economic burden on the government or its services to materially impair the usefulness or efficiency of the organization, or to materially restrict the performance of its duties.¹⁴

What makes the *Wachovia* factors test difficult is that the presence or absence of any of the foregoing factors is not dispositive and “the presence of all is not required, to constitute any given agency an instrumentality.”¹⁵ Moreover, the court in *Wachovia* concluded that, in general, an entity “public in nature, created and wholly owned by the government for the convenient prosecution of its governmental functions, existing at the will of its creator, is an instrumentality of government.”¹⁶

According to the Department, the agency’s policy and practice is to utilize only the control test, unless a situation arises where the facts of a case makes it unclear whether the test is met. After a fairly exhaustive review of both the Department’s informal policy letters and declaratory orders issued on this point, the undersigned administrative law judge is not certain that’s entirely true.¹⁷ Nevertheless, there is some case precedent to suggest our state relies upon the *Orleans* control test over *Wachovia*.¹⁸ Moreover, the *Wachovia* decision itself stands for the notion that a government body must have a high level of control over an organization to qualify it as an instrumentality. Considering the *Wachovia* factors alone is not particularly useful when reaching a conclusion on whether an entity qualifies as an instrumentality of government. The undersigned thus concludes primarily utilizing the *Orleans* control test, while considering the

¹¹ *United States v. Orleans*, 425 U.S. 807, 808 (1976).

¹² *Id.*

¹³ 2 S.E.2d 592 (North Carolina 1939).

¹⁴ *Id.* at 596.

¹⁵ *Id.*

¹⁶ *Id.* at 595.

¹⁷ While the Department’s informal policy letters may not be considering binding legal authority, certainly they offer insight into the agency’s standard policy and practice on a given issue. See e.g. *Dvorak to Ankeny Community Foundation*, Policy Letter 15300063, September 2, 2015 (utilizing *Wachovia* test); but see also *DeVries to Redacted Entity*, Policy Letter 06300004, December 22, 2005 (utilizing *Orleans* control test as primary indicator and *Wachovia* test for “borderline cases.”).

¹⁸ See *South Central Iowa Production Credit Ass’n vs. Scanlan*, 380 N.W.2d at 701 (utilizing the *Orleans* control test to determine “federal instrumentality” status).

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Wachovia factors when the control test is inconclusive leads to the most practical results while also following legal precedent.

Both parties have cited previous decisions of the Department as persuasive authority. The Department's declaratory decision filed on January 25, 2021 in the *Matter of Heartland Insurance Risk Pool* is the most recent and instructive.¹⁹

In that case, a nonprofit municipal corporation was formed by ten counties pursuant to Iowa Code chapter 28E for the sole purpose of creating a loss control program exclusive to its county members. Membership was limited to Iowa counties, and run by a board of trustees consisting of a county supervisor or auditor appointed by each of its members, who were agents authorized to act on a member county's behalf. The entity was funded entirely by the members. The Department utilized both the *Orleans* control and *Wachovia* factors tests to reach the conclusion the entity qualified as an instrumentality of government.

In this case, ISAC contends it satisfies said control test. It argues ISAC is subject to state legislative control as it is referenced many times throughout the Iowa Code.²⁰ Moreover, it argues its membership is comprised of county officials, employees, and counties themselves, and that its Board of Directors consists entirely of county officials acting in their professional capacities. Conversely, the Department argues ISAC fails said control test. The state asserts counties themselves have no voting rights within ISAC, nor do they have authority to appoint individuals to the Board of Directors, with which the entire control of ISAC's affairs is vested. Rather, ISAC's Board of Directors is comprised of individuals appointed by the entity's affiliated organizations.

ISAC's governance structure sets it apart from an entity like the subject of *In the Matter of Heartland Insurance Risk Pool*. In the latter, each county member appointed an elected official to the organization's governing body to act on their behalf. Whereas in ISAC's situation, the "affiliated organizations" select the individuals serving on its governing body. It is somewhat unclear from this record the qualifications for membership to each of ISAC's affiliated organizations. Moreover, the added layer between the member counties and ISAC's governing body—the Board of Directors—shows the counties themselves do not possess the requisite detailed, physical control over the organization's day-to-day activities in order to qualify as an instrumentality as set forth in *Orleans*.

Expounding further, even if the *Orleans* control test was not conclusive for this case, the *Wachovia* factors are not particularly helpful here. ISAC only meets some of the *Wachovia* factors. The organization was not created by county government itself, but it was founded by multiple county officials. It is not wholly owned by the government. The organization is not operated for profit. There is not enough evidence in the record to support the argument imposing sales tax upon ISAC would create a legitimate economic burden on the counties. Moreover, while some of ISAC's operations appear to qualify as an "essential governmental function," such as its self-funded insurance pools and mental health case management systems, other offerings,

¹⁹ 2021-WL 1087129 (January 25, 2021).

²⁰ See e.g. I.C.A. 331.401 (regarding membership dues); I.C.A. 11.6(9) (regarding audits); I.C.A. 147A.2 (regarding appointments to the EMS Advisory Council).

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such as continuing education programs, professional conferences, publications, and scholarship fund, are for the personal benefit and/or professional development of the participating individuals. It is clear from the record that ISAC's educational and professional support were incredibly helpful to its county official and employee members in their professional capacities and without ISAC they would be forced to find it elsewhere. That does not, however, equate to an "essential government function."

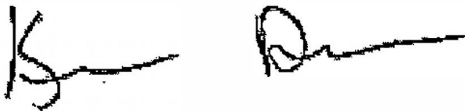
Accordingly, in considering the applicable law under the facts of this case, the undersigned concludes ISAC has not shown it is exempt from paying sales tax as an instrumentality of government. This conclusion is also supported by Iowa law requiring that exclusions from taxation be "construed strictly against the taxpayer and liberally in favor of the taxing body."²¹

For these reasons, the Department's decision must be affirmed.

ORDER

The Department's action is hereby **AFFIRMED**. The Department shall take any action necessary to implement this decision.

Dated this January 13, 2022.


Kristine M. Dreckman
Administrative Law Judge

cc: Katherine Penland/Adam Humes (via email); K. Dwayne Vande Krol/ Thomas Goodhue (via email)

²¹ See *Ranninger v. Iowa Dept. of Revenue and Finance*, 746 N.W.2d 267, 269 (Iowa 2008) (rejecting a taxpayers broad interpretation of a phrase in favor of the Department's narrow definition); citing *Iowa Auto Dealers Ass'n v. Iowa Dept. of Revenue*, 301 N.W.2d 760, 762 (Iowa 1981); accord *Heartland Lysine, Inc. v. State*, 503 N.W.2d 587, 588-9 (Iowa 1993).

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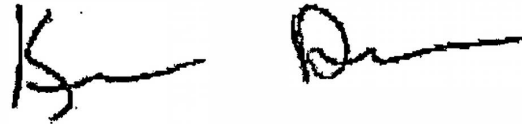
NOTICE

Pursuant to 701 Iowa Administrative Code 7.17(8)(d), this order becomes the final order of the Department for purposes of judicial review or rehearing unless a party files an appeal to or review on motion of the director with 30 days of the date of this order, including Saturdays, Sundays and legal holidays, of the date of this Proposed Decision to file an appeal to the Director of the Department of Revenue. The appeal shall be directed to:

Office of the Director
Iowa Department of Revenue
Hoover State Office Building
Des Moines, Iowa 50319

Case Title: IOWA STATE ASSOCIATION OF COUNTIES
Case Number: 20IDR0044
Type: Proposed Decision

IT IS SO ORDERED.

A handwritten signature in black ink, appearing to be 'K. Dreckman', written over a horizontal line.

Kristine Dreckman, Administrative Law Judge