

CAUSE NO. D-1-GN-18-007023

POINTSMITH POINT-OF-PURCHASE	§	IN THE DISTRICT COURT OF
MANAGEMENT SERVICES, LP	§	
Plaintiff,	§	
	§	
v.	§	
	§	TRAVIS COUNTY, TEXAS
GLENN HEGAR,	§	
COMPTROLLER OF PUBLIC	§	
ACCOUNTS OF THE STATE OF TEXAS;	§	
THE OFFICE OF THE COMPTROLLER	§	
OF PUBLIC ACCOUNTS;	§	
KEN PAXTON, ATTORNEY	§	
GENERAL OF THE STATE OF TEXAS;	§	
AND THE OFFICE OF THE ATTORNEY	§	
GENERAL OF THE STATE OF TEXAS	§	345TH
Defendants.	§	JUDICIAL DISTRICT

**PLAINTIFF’S ORIGINAL PETITION AND
REQUEST FOR DISCLOSURE**

TO THE HONORABLE JUDGE OF THIS COURT:

COMES NOW Pointsmith Point-of Purchase Management Services, LP (“Pointsmith”), Plaintiff, complaining of the above-listed Defendants (collectively the “Comptroller”). In support of its claim, Pointsmith will show the Court the following:

DISCOVERY CONTROL PLAN

1. Pointsmith elects to conduct discovery under Level 3 of Rule 190.4, Texas Rules of Civil Procedure.

PARTIES

- 2. Pointsmith is a Texas corporation with its headquarters in Katy, Texas.
- 3. Defendant Glenn Hegar is the Comptroller of Public Accounts of the State of Texas and is the public official charged with the duty of collecting the Texas sales and use tax.

4. Defendant Glenn Hegar is sued in his official capacity as Comptroller of Public Accounts of the State of Texas. The Defendant Comptroller may be served at the Lyndon Baines Johnson State Office Building, 111 East 17th Street, Austin, Travis County, Texas, 78701.

5. Defendant Office of the Comptroller of Public Accounts may also be served at the Lyndon Baines Johnson State Office Building, 111 East 17th Street, Austin, Travis County, Texas, 78701.

6. Defendant Ken Paxton is the Attorney General of the State of Texas.

7. Defendant Ken Paxton is sued in his official capacity as Attorney General of the State of Texas. The Defendant Attorney General may be served at the Price Daniel Building, 209 West 14th Street, 8th Floor, Austin, Travis County, Texas, 78701.

8. Defendant Office of the Attorney General of the State of Texas may also be served at the Price Daniel Building, 209 West 14th Street, 8th Floor, Austin, Travis County, Texas, 78701.

JURISDICTION AND VENUE

9. Pointsmith brings suit under Texas Tax Code §§ 112.052 *et seq.* and Texas Government Code §§ 403.203 *et seq.* to recover from Defendants in their respective official capacities and from the State of Texas \$651,132.64, which represents the portion of Pointsmith's Protest Payment of \$772,120.45 made on October 22, 2018 that Pointsmith estimates is attributable to its fulfillment service. Although Pointsmith desires to challenge only the Comptroller's assessment relating to its fulfillment service and to pay the balance of the assessment directly to the Comptroller without contest, the Comptroller has refused to provide Pointsmith with an updated assessment that accurately reflects interest accrued during the

pending administrative redetermination and to allocate that interest between fulfillment and non-fulfillment issues. Thus, Pointsmith made its own calculation of the revised assessment and paid that amount under protest. Pointsmith intends to contest only the portion of the Protest Payment relating to its fulfillment service, which it estimates to be \$651,132.64. However, if the court ultimately determines that the portion of the Protest Payment attributable to Pointsmith's fulfillment service is higher than the amount stated here, Pointsmith's protest extends to the amount ultimately identified as the sum attributable to this sole contested issue, limited to \$772,120.45, which is the full amount of the Protest Payment.

10. The payment made under protest has been made under duress on the demand of Defendant Glenn Hegar, Comptroller of Public Accounts of the State of Texas, as taxes claimed by the State of Texas under the terms and provisions of Chapter 151 of the Texas Tax Code.

11. Pointsmith also brings suit under the Texas and United States Constitutions, Texas Civil Practice and Remedies Code Chapter 37, Texas Government Code Chapter 2001, and the *ultra vires* doctrine.

12. Pointsmith is registered with the Texas Secretary of State to do business in Texas.

13. Pointsmith has complied with all jurisdictional prerequisites necessary to file this suit.

14. Pointsmith submitted with its payment under protest a written protest letter stating the reasons it is entitled to recover the payment. Pointsmith attaches the protest letter, a copy of its protest payment, and related attachments as **Exhibit A** and incorporates **Exhibit A** by reference as though it was duly set forth at length herein.

15. Ninety days have not elapsed since Pointsmith made its payment under protest.

16. The Travis County District Courts have exclusive, original jurisdiction over this case pursuant to Texas Tax Code § 112.001, as well as the Texas and United States Constitutions, Chapter 37 of the Texas Civil Practice and Remedies Code, Chapter 2001 of the Texas Government Code, and the *ultra vires* doctrine.

FACTS

17. Pointsmith is located in Katy, Texas and has two business lines, both of which relate to point-of-purchase marketing.

18. Pointsmith prints and sells point-of-purchase marketing materials.

19. Pointsmith provides fulfillment services for point-of-purchase marketing materials.

20. Pointsmith provides each of its services independently of each other.

21. Point-of-purchase marketing means the placement of promotional signs or advertisements at locations where consumers pay for products and services (such as gas station pumps and counters and the windows at a drive-through restaurant). It also includes the provision of give-away items to consumers to generate brand recognition or to promote a particular product or service.

22. Pointsmith's fulfillment service consists of: (1) leasing storage space within Pointsmith's facility for a customer to store its advertising materials; (2) handling (*i.e.*, retrieving customer-selected items from the customer's leased storage space and packing them into boxes); and (3) shipping the customer's boxed items as instructed by the customer.

23. Pointsmith prints custom marketing materials for which unrelated third-parties provide fulfillment services.

24. Pointsmith provides fulfillment services for items printed or produced by unrelated third-parties.

25. Pointsmith operates its two business lines in distinct and separate areas of its facility, and Pointsmith does not use the same employees, supervisors, or business assets across these lines of business.

26. Pointsmith's customers are large, multi-unit companies, predominantly within the retail gasoline, convenience store or fast casual dining industries. Its major customers include Murphy Oil, Popeye's, Citi Cards, Mattress Firm, and Shell Oil and their franchisees.

27. Pointsmith's customers own or franchise stores. These customers use point-of-purchase marketing at their stores' locations both in and outside of Texas.

28. Approximately 74% of Pointsmith's customers' stores are located outside the state of Texas.

29. Pointsmith's customers typically require Pointsmith to bid for work.

30. Pointsmith's customers may solicit bids for printing only. Pointsmith's customers may solicit bids for fulfillment services only. Pointsmith's customers may solicit bids for both printing and fulfillment services.

31. Regardless of whether a customer solicits bids for printing only, for fulfillment services only, or for both, Pointsmith prepares separate bids and prices for each type of work. Pointsmith's prices do not vary based upon whether both are purchased or not.

32. Pointsmith prints custom marketing materials with the content and in the sizes and quantities ordered by its customers.

33. For example, Murphy Oil orders printed decals to cling to the entrance door of its convenience stores to advertise that lottery tickets are sold at certain locations. Similarly, Murphy Oil may hire Pointsmith to print signs to be placed on the top of gas pumps announcing a new type of engine fuel.

34. As soon as Pointsmith prints a customer's marketing materials, the customer will direct Pointsmith to deliver the materials to the customer either at Pointsmith's shipping dock for pickup and shipment by common carrier or to the customer's leased warehouse space.

35. Title to the materials passes to the customer at the location to which the customer directs delivery (*i.e.*, Pointsmith's shipping dock or the customer's leased warehouse space).

36. Possession of the materials passes to the customer at the location to which the customer directs delivery (*i.e.*, Pointsmith's shipping dock or the customer's leased warehouse space).

37. When materials are delivered to Pointsmith's dock, they are immediately loaded and shipped to individual stores.

38. Pointsmith's customers bear the risk of loss of the printed materials once Pointsmith delivers the materials to the customer at Pointsmith's loading dock or to the customer's leased warehouse space.

39. Pointsmith's customers lease warehouse space from Pointsmith by the square foot. Pointsmith's customers own all of the marketing materials that they store there.

40. Pointsmith's customers purchase some of their marketing materials from unrelated vendors and some from Pointsmith.

41. Pointsmith's customers are responsible for insuring the materials that they store in the leased warehouse space. The customers are the named insured on their policies.

42. Pointsmith's customers are also responsible for rendering to the Harris County Appraisal District ("HCAD") the value of the marketing materials for property tax.

43. HCAD requires Pointsmith to identify the customers that own the marketing materials so that HCAD may assess the property taxes against those customers. Pointsmith complies.

44. Pointsmith's customers have the right to inspect the marketing materials they store at Pointsmith's facility, and customers often exercise their rights of inspection.

45. Acting upon its customers' instructions, Pointsmith will gather specific advertising materials selected by the customer from the customer's leased warehouse space, place them into boxes (aka "pick and pack" or "handling"), and ship the boxes to the stores as directed by the customers.

46. When providing fulfillment services, Pointsmith does not package together and send to a single store all of the items sold under a single customer print invoice.

47. When providing fulfillment services, Pointsmith does not place all of the individual items from a single print invoice into different boxes and ship them to different stores.

48. Rather, when providing fulfillment services, Pointsmith places the items from a particular sale into boxes with items from other sales and/or items produced by third parties and then packages and sends them to different stores at different times.

49. The items for which a customer leases storage space within Pointsmith's facility may remain there for months to years before the customer directs Pointsmith to retrieve and pick

them for a fulfillment order. Thus, fulfillment services for Pointsmith-printed materials may lag months to years behind the print sales of those materials.

50. If a customer determines that certain advertising materials stored in the warehouse have become outdated, the customer will direct Pointsmith to discard them. The customer controls disposal of its property once Pointsmith stores it in the customer's leased warehouse space.

51. The marketing materials that customers store in the leased space are highly-customized, branded items that hold no value for Pointsmith and for which Pointsmith has no incentive to bear the burdens of ownership.

52. Pointsmith prepares and sends separate invoices for its charges for print sales and for fulfillment services.

53. Printing charges are based on the quantities and prices of items printed, and account for the cost of raw materials (such as blank poster sheets and printing ink), the labor employed to print and deliver the items to the customer, and other expenses, such as the depreciation of printing presses and copiers

54. In contrast, Pointsmith's fulfillment charges are based upon the square footage of rented warehouse space, packaging labor and box costs, and any third-party shipping costs that Pointsmith incurs.

55. Fulfillment pricing does not vary between the storage, packaging, and shipment of Pointsmith-printed items and third party-produced items.

56. Pointsmith does not provide discounts when its customers purchase both printing and fulfillment together. Its prices do not vary regardless of whether a customer seeks one or both services.

57. When Pointsmith delivers a customer's printed materials to either its dock or to the warehouse space leased by its customer, Pointsmith invoices the customer for the price of the printed materials and, absent an applicable exemption, charges Texas sales tax on the full price (including freight).

58. Approximately 74% of Pointsmith's printed products are shipped to stores located outside of Texas.

59. Pointsmith charges sales tax on every item at the time the customer directs its delivery to Pointsmith's dock or to the customer's lease warehouse space, regardless of the ultimate destination of the item.

60. Upon delivery of the printed marketing materials as directed by the customer to either Pointsmith's dock or the warehouse space, Pointsmith reduces its inventory account for the cost of the materials and records the cost of the materials as a cost of goods sold. Likewise, the customer records the prices paid for the marketing materials on its books as inventory.

61. Pointsmith does not charge Texas sales and use tax on its fulfillment services.

62. The Comptroller has audited Pointsmith for every Texas sales and use tax period from 2000 through 2013, issuing an assessment for each period.

63. Throughout these audits, Pointsmith has provided the Comptroller with unfettered access to all of its books and records. Since at least mid-2004, the Comptroller's auditors have spent numerous hours onsite at Pointsmith's business facilities touring the property and

interviewing its employees to gain an understanding of the nature of its business and Texas sales and use tax practices.

64. Pointsmith has challenged each audit assessment either through the administrative redetermination process or by district court protest suit. Thus, Pointsmith has been actively litigating against the Comptroller for 15 years.

65. For the three audits spanning the 2003 through 2013 sales tax periods, the Comptroller imposed Texas sales and use tax on Pointsmith's fulfillment services.

66. Pointsmith originally challenged the 2003-2007, the 2007-2010, and 2010-2013 audit periods through the administrative redetermination process.

67. After losing the administrative hearing for the 2003-2007 audit period, Pointsmith proceeded to challenge the assessment in district court through a Texas Tax Code Chapter 112 protest suit.

68. The later audit periods remained in the administrative redetermination forum while the district court suit proceeded to trial.

69. In December of 2017, Pointsmith tried its protest suit on the merits to Travis County District Court Judge Timothy Sulak. The trial lasted four days and included testimony from three witnesses and over 200 exhibits.

70. In January of 2018, Judge Sulak entered judgment in Pointsmith's favor. *See Exhibits 2 and 3 to Exhibit A.* The Comptroller ordered the trial transcript, but ultimately chose not to appeal. Thus, the judgment became final.

71. Shortly thereafter, Pointsmith asked the Comptroller to resolve the subsequent audits by applying the ruling of the district court judgment. *See Exhibit 4 to Exhibit A.*

72. Pointsmith and the Comptroller confidentially resolved the smaller 2007-2010 audit period.

73. For the 2010-2013 audit period at issue here, Pointsmith proposed to the Comptroller a Rule 11 Agreement wherein Pointsmith would agree provide documents like those used to prove its case-in-chief at trial if the Comptroller would agree to apply the district court ruling and treat Pointsmith's fulfillment service as non-taxable once Pointsmith established no material difference in facts. *See Exhibit 5 to Exhibit A.* The Comptroller refused, stating that the audit was correct.

74. Then, the Comptroller sought to initiate yet another audit of Pointsmith for the Texas sales and use tax periods following those at issue here. Only when counsel for Pointsmith sent to the head of the audit division a letter detailing the Comptroller's repetitive assessments of Pointsmith, notwithstanding the trial court's final judgment, and the impropriety of auditing Pointsmith while this protest litigation was ongoing did the Comptroller agree to delay the audit, but only for a period of one year. *See Exhibit 6 to Exhibit A.*

75. Notwithstanding the lack of any material change in Pointsmith's business operations between the audit period litigated in district court and the period presently at issue, the Comptroller has refused to follow Judge Sulak's district court judgment and, instead, is forcing Pointsmith to re-litigate the taxability of its fulfillment service through this protest suit because the Comptroller disagrees that Judge Sulak's letter ruling and judgment "is a decision on the merits" because "the judgment contains no analysis of law or conclusions of law." *See Exhibits 7 and 8 to Exhibit A.*

76. Thus, the Comptroller has determined that a judgment in a protest suit that orders the Comptroller to return the taxpayer's protest payment occurs without any determination of taxability. According to the Comptroller, when the Comptroller imposes an audit assessment claiming that a taxpayer failed to collect tax on a service and the taxpayer challenges that assessment – arguing that its service is not taxable – and prevails, the Comptroller's position is that the court's ruling is not a decision on the merits and therefore has no effect on other periods.

77. Over the last 15 years, the Comptroller has forced Pointsmith to divert thousands of hours of employee time (largely that of high-level executives) and spend hundreds of thousands of dollars in professional fees to facilitate Comptroller audit examinations and then litigate his unjustified assessments.

78. As of the January 2018 judgment, the law and resulting application to Pointsmith's business was determined. Thus, this entire protest suit – which, once again, concerns the taxability of Pointsmith's fulfillment service – is completely unnecessary since Judge Sulak applied the governing law to Pointsmith's unchanged facts.

79. In light of the Comptroller's refusal to enter into the proposed Rule 11 Agreement and his inability to point to any material change in Pointsmith's business operations, his claim that additional tax is due constitutes nothing more than an attempt to circumvent Judge Sulak's ruling on the law.

80. As a result, under duress, Pointsmith is forced to bring this protest suit to prevent the assessment from becoming final, which would then allow the Comptroller to commence collection efforts for tax that is not lawfully due.

81. Pointsmith has followed the jurisdictional steps outlined by James Arbogast and Jack Hohengarten regarding proper dismissal of a pending administrative redetermination hearing to pursue a district court protest suit. *See Exhibits 9 and 10 to Exhibit A.* However, due to the Comptroller's refusal to provide Pointsmith with a revised assessment stating the amount of tax, penalty, and interest presently assessed for the audit period, Pointsmith was forced to make its own calculation of the required protest payment.

82. Pointsmith hereby incorporates by reference as though duly set forth at length the entire administrative file for Comptroller Hearing Number 113,938, including correspondence between counsel for Pointsmith and the Comptroller.

83. Pointsmith's protest letter expressly allowed the Comptroller thirty days from its date to reconsider his position that he's entitled to retry the same issue for the same taxpayer/plaintiff when a Travis County judge recently issued a decision on the issue for the same taxpayer in a prior audit. The Comptroller never alleged that the underlying facts may have changed. Instead, the Comptroller states that he doesn't consider Judge Sulak's decision and related order to constitute a decision on the merits, despite being furnished proof to the contrary on several occasions. The Comptroller refused to reconsider his position within the thirty-day period. As a result, Pointsmith files this protest suit seeking numerous remedies, including a recovery of its protest payment and accruals, declaratory relief, attorney's fees, and sanctions.

84. The Comptroller's assessment is in error for the reasons stated below.

THE COMPTROLLER MUST MAKE PRIMA FACIE SHOWING OF TAXABILITY

85. The Comptroller has alleged that Pointsmith's fulfillment services are taxable under Chapter 151 of the Texas Tax Code.

86. There is no presumption that services are taxable for purposes of the Texas sales and use tax. Under his policies, the Comptroller has the burden to establish a prima facie case that Pointsmith provides a taxable service when it provides fulfillment services.

RULES OF CONSTRUCTION FAVOR POINTSMITH

87. Doubts as to taxability must be construed in Pointsmith's favor. "[S]tatutes imposing a tax must be strictly construed against the taxing authority and liberally construed in favor of the taxpayer." *Austin Eng'g Co. v. Combs*, No. 03-10-00323-CV, 2011 WL 3371557, at *5 (Tex. App.—Austin 2011, no pet.) (mem. op.); *Statistical Tabulating Corp. v. Bullock*, 538 S.W.2d 259, 261 (Tex. Civ. App. Austin 1976, *aff'd*, 549 S.W.2d 166, 169) (Tex. 1977); *see also Roark Amusement & Vending, L.P. v. Combs*, No. 03-10-00105-CV, 2011 WL 255535, at *11-12 (Tex. App.—Austin 2011, pet. granted); *see also; Geomap Co. v. Bullock*, 691 S.W.2d 98, 100 (Tex. App.—Austin 1984, writ ref'd n.r.e).

88. This case concerns whether Pointsmith's fulfillment service is subject to Texas sales and use tax, not whether it is exempt from the tax.

GROUND

I. Pointsmith's Fulfillment Service is Not Taxable.

89. Texas imposes sales tax on "each sale of a taxable item in this state." Tex. Tax. Code § 151.051.

90. Taxable items include both tangible personal property and taxable services. Tex. Tax. Code § 151.010.

91. “Taxable services” are limited to a statutory list of seventeen (17) categories, none of which include fulfillment or its individual components of storage, handling, and shipping. *See* Tex. Tax Code § 151.0101 (storage is only taxable for motor vehicles).

92. Thus, as previously held by Judge Sulak on similar facts, Pointsmith’s fulfillment service is not taxable.

II. Pointsmith’s Fulfillment Charges are Not Taxable as “Part of the Sale” of Printed Materials.

93. An otherwise non-taxable service may become taxable if it is “part of the sale” of a taxable item. *See* Tex. Tax Code § 151.007 (defining the “sales price” of a taxable item to be the total amount for which the taxable item is sold without a deduction for various costs, such as the cost of the transportation of tangible personal property or a service that is “a part of” the sale).

94. The sale of printed materials is taxed as the sale of tangible personal property. *See May Department Stores Co. v. Strayhorn*, No. 03-03-00729-CV, 2004 LEXIS 7681 at *19 (Tex. App.—Austin Aug. 26, 2004) (mem. op.).

95. The Comptroller incorrectly alleges that Pointsmith’s fulfillment services are taxable because they are “part of the sale” of materials that Pointsmith prints.

96. For Texas sales and use tax purposes, a sale is (1) the transfer of title *or* possession (2) of a taxable item (3) when done or performed for consideration. *See* Tex. Tax Code § 151.005.

97. Pointsmith satisfies all conditions of a sale at the time it delivers the printed materials to its customers at its shipping dock or to its customers' leased warehouse space.

98. Pointsmith transfers both title and possession (actual or constructive) of the taxable printed items to its customers, and its customers become obligated to pay the consideration due.

99. Thus, Pointsmith's sale of printed materials is complete before any fulfillment services are provided and the Comptroller has improperly assessed tax on Pointsmith's fulfillment sales.

III. Pointsmith's Fulfillment Services Are Not Taxable as the "Delayed Assembly and Transportation" of Printed Materials.

100. The Comptroller mischaracterizes Pointsmith's fulfillment services as delayed assembly and transportation of printed materials, which is contrary to the facts of Pointsmith's business, the trial judge's earlier determination, and the Comptroller's own guidance.

101. A charge for assembly is considered part of a manufacturing process and is taxable.

102. "Assembly" is defined under the tax laws as "the labor to connect component parts into a finished product; it is the final stage in the manufacturing process." *See, e.g.* Comptroller Letter Ruling, STAR No. 8805L09004G01 (May 17, 1988).

103. Pointsmith's fulfillment activities do not involve connecting component parts into a finished product. The individual items Pointsmith places into a delivery box are already complete and retain their separate identities.

104. Pointsmith's "manufacturing" of printed items is complete when the items come off the press in a state that meets the customer's specifications.

105. The activities of gathering specific advertising materials and placing them into boxes (“pick and pack,” or “handling”) comprise one stage in the process of completing a fulfillment order and do not constitute taxable assembly labor.

106. The Comptroller previously confirmed in a letter ruling that pick-and-pack services, for which a handling fee was charged, were not taxable. Comptroller Letter Ruling, STAR No. 9809831L (Sept. 17, 1998).

107. Further, Pointsmith’s fulfillment service is not taxable as delayed transportation or delivery of the items Pointsmith prints.

108. As a threshold matter, transportation is not a taxable service. The Tax Code does not classify transportation as a taxable service in Section 151.0101, and Comptroller Rule 3.303 recognizes that third-party transportation charges are not taxable.

109. Under Chapter 151 of the Texas Tax Code, the “sales price” includes the total amount for which a taxable item is sold without a deduction for the cost of transportation.

110. “Transportation” means “the movement of goods from the possession of the seller to the purchaser.” *Spencer Gifts, Inc. v. Bullock*, 766 S.W.2d 593, 596 (Tex. App.—Austin 1989, no writ.) (defining “transportation” in the sales tax context).

111. Thus, the charge for the movement of a product from the seller’s possession to the buyer’s possession is part of the taxable price of the product when the movement is connected to the sale of that product. *See id.*

112. Comptroller Rule 3.303 explains that charges for transportation or delivery, both before and after the sale, are taxable even if stated separately from the sales price of a taxable item, because they are “connected to the sale.”

113. The charges for transportation or delivery are not taxable if they are not connected to the sale.

114. Where a taxpayer manufactures, sells, and installs an item for its customer, and then later moves and stores the item temporarily at the customer's direction, the Comptroller has ruled that the charges for the movement and storage are not subject to sales tax. *See* Comptroller Policy Letter, STAR No. 9607L1426A12 (July 9, 1996).

115. Once Pointsmith sells the printed materials and delivers them to the customers' leased warehouse space, any subsequent shipment to the franchised or company-owned stores is not "transportation" within the meaning of the statute, because it is not the movement of Pointsmith's inventory from Pointsmith's possession to the customer's; instead, it is movement from the customers' possession to other locations as directed by the customers.

116. The Comptroller has ruled that constructive possession satisfies the possession element of a sale and that actual possession is not required. *See* Comptroller Hearing No. 19,581, STAR No. 8804H0883G01 (April 4, 1988). Thus, the activity of transportation occurs when a seller transfers the items sold to the location directed by the buyer, even if it is to warehouse space leased by the buyer from the seller.

117. Fulfillment cannot constitute the delayed transportation or delivery of the items Pointsmith prints, because Pointsmith has already transported those items and delivered them to the customer's leased warehouse space well before the customer directs them to be shipped elsewhere.

118. Pointsmith's delivery charge for the initial movement of the printed materials is imbedded in the sales price of the printed materials. Pointsmith charges sales tax on the full

charge for the printed materials. Thus, Pointsmith charges sales tax on the transportation of the printed materials.

119. The fulfillment services are not “a part of” Pointsmith’s print sale, because the print sale has already concluded and been appropriately taxed before the fulfillment work begins.

120. Pointsmith’s fulfillment service is not taxable as delayed assembly and transportation. Therefore, the Comptroller has improperly assessed tax on Pointsmith’s fulfillment sales.

IV. Pointsmith’s Fulfillment Service Should Not be Taxes as Part of Print Transactions Because it is Independently Desired and Provided.

121. When the purchase of a nontaxable service is combined with the purchase of a taxable item, but each transaction is independently desired and independently provided, there is a mixed transaction in which neither element is “incident” to the other. *Rylander v. San Antonio SMSA Partnership*, 11 S.W.3d 484, 487-488 (Tex. App.—Austin 2000, no pet.).

122. When there is a fixed and ascertainable relationship between the value of the article and the value of the services rendered, and each is a consequential element capable of a separate and distinct transaction, the elements must be analyzed as separate transactions for tax purposes. *Id.*

123. Even when taxable items and non-taxable services are bundled or related, non-taxable services remain non-taxable when two conditions exist. First, the customer must independently desire the separate furnishing of the taxable items and the non-taxable services. Second, the seller must independently and separately sell the taxable items and the non-taxable services. *Id.*

124. Pointsmith's print services and fulfillment services are independently desired and independently provided. Neither is incident to the other. Pointsmith engages in separate and distinct transactions for each.

125. Therefore, the taxability of Pointsmith's print sales and the taxability of Pointsmith's fulfillment sales should be evaluated independently, and the two should be analyzed as separate transactions, with the fulfillment transaction retaining its non-taxable character.

V. If Pointsmith's Fulfillment Service is Taxed as Part of Print Sales, Then Pointsmith Has Over-Collected and Remitted Tax on Print Items Sent Out of State.

126. Texas may only tax the sale of a taxable item in *this state*. See Tex. Tax Code §151.051 (emphasis added).

127. Tangible personal property (*e.g.*, a printed item) shipped to a point outside of Texas is not subject to Texas sales and use tax. See Tex. Tax Code § 151.330.

128. Even though 74% of Pointsmith's printed products are ultimately bound for locations outside of Texas, Pointsmith taxes them, absent an applicable exemption, at the time they are delivered to the customer at Pointsmith's facility because that is where Pointsmith and its customers conclude the sale.

129. If Pointsmith's sale continued through to the items' ultimate destinations, as alleged by the Comptroller, then Pointsmith has vastly over-collected Texas sales and use tax on the charge for printed items and is entitled to recover its entire protest payment.

VI. The Comptroller Has Violated Pointsmith's Right to Equal Taxation.

130. The Comptroller's attempt to tax Pointsmith's fulfillment service violates the equal protection clauses of the United States and Texas Constitutions.

131. The Fourteenth Amendment to the United States Constitution grants to all citizens equal protection under the law. The Texas Constitution, Article VIII, Section 1, provides for equality and uniformity in taxation.

132. The Comptroller has treated Pointsmith differently from a large class of similarly-situated taxpayers who provide fulfillment services by imposing Texas sales and use tax on Pointsmith's sales in an arbitrary and discriminatory manner. The Comptroller treats Pointsmith differently by imposing Texas sales and use tax on its fulfillment service when he does not impose tax on fulfillment houses that do not sell or print taxable items.

133. The Comptroller's disparate treatment of Pointsmith is not rationally related to any legitimate governmental objective.

134. Therefore, the assessment should be reduced to zero because the Comptroller has violated Pointsmith's right to equal protection and equal and uniform taxation.

VII. Pointsmith Is Entitled to Declaratory Relief Under the UDJA.

135. Chapter 37 of the Civil Practice and Remedies Code affords relief from uncertainty and insecurity with respect to rights, status, and other legal relations. Tex. Civ. Prac. & Rem. Code § 37.002.

136. A person whose rights, status, or other legal relations are affected by a statute may have determined any question of construction or validity arising under the statute and obtain a declaration of rights, status, or other legal relations thereunder. Tex. Civ. Prac. & Rem. Code § 37.004.

137. Texas Civil Practice and Remedies Code Section 37.006 waives governmental immunity from suit. *City of El Paso v. Heinrich*, 284 S.W.3d 366, 373 n.6 (Tex. 2009).

138. Pointsmith's rights, status, and other legal relations are affected by the Texas sales and use tax provisions cited above and, therefore, Pointsmith may have determined questions of construction or validity arising under these statutes and obtain a declaration of its rights, status, or other legal relations thereunder.

139. Therefore, Pointsmith seeks the following declarations, as well as costs and reasonable and necessary attorney's fees as are equitable and just, under Chapter 37 of the Civil Practice and Remedies Code:

- a. Fulfillment services are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- b. The charges for leasing storage space for customers to store tangible personal property – a component of Pointsmith's fulfillment service – are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- c. The charges for handling (picking customer-selected items from the customer's leased storage space, packing them into boxes, and sealing the boxes) – a component of Pointsmith's fulfillment service – are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- d. The charges for shipment of customers' boxed items – a component of Pointsmith's fulfillment service – are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- e. Pointsmith's fulfillment services are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.

- f. None of the individual components of Pointsmith’s fulfillment service constitute “a part of the sale” of a taxable item under Texas Tax Code § 151.051, 151.010 and 151.0101.
- g. Pointsmith’s fulfillment service is not a service that is “a part of the sale” of a taxable item under Texas Tax Code § 151.007.
- h. None of the individual components of Pointsmith’s fulfillment service are “a part of the sale” of a taxable item under Texas Tax Code § 151.007.
- i. Pointsmith’s sale of custom printed materials and its provision of fulfillment services are distinct and identifiable.
- j. Pointsmith’s sale of custom printed materials and its provision of fulfillment services are readily separable.
- k. Pointsmith’s sale of custom printed materials and its provision of fulfillment services are independently desired.
- l. Pointsmith’s sale of custom printed materials and its provision of fulfillment services are independently provided.

140. The need for declaratory relief, in addition to that provided by Pointsmith’s protest suit, is evidenced by the Comptroller’s refusal to follow the district court judgment and to apply it to Pointsmith’s subsequent periods.

141. Pointsmith seeks the court’s declarations to establish the proper tax treatment for periods other than those for which it made the protest payment.

VIII. Pointsmith Is Entitled to Relief from Comptroller Hegar's *Ultra Vires* Conduct.

142. The Texas Supreme Court has long recognized that governmental immunity does not bar claims alleging that a governmental officer acted *ultra vires*, or without legal authority, in carrying out his duties. *Houston Belt & Terminal Ry. Co. v. City of Houston*, 487 S.W.3d 154, 157-58 (Tex. 2016).

143. A government officer with some discretion to interpret and apply a law may nonetheless act without legal authority and, thus, *ultra vires* if he exceeds the bounds of his granted authority or if his acts conflict with the law itself. *Id.* at 158.

144. Comptroller Hegar has the authority to collect the Texas sales and use tax and some – but not absolute – discretion to administer and to enforce the tax. *See, e.g.*, Tex. Tax Code §§ 111.001 and 111.002; *Houston Belt*, 487 S.W.3d at 163 (“[G]overnmental immunity bars suits complaining of an exercise of *absolute* discretion but not suits complaining of . . . an officer’s exercise of judgment or *limited* discretion without reference to or in conflict with the constraints of the law authorizing the official to act. . . . [A] public officer has no discretion or authority to misinterpret the law.”).

145. Comptroller Hegar is bound by the United States Constitution, the Texas Constitution, and the laws enacted by the Texas Legislature. *See, e.g.*, Tex. Tax Code §§ 111.001 and 111.002. His taxing determinations are also subject to judicial review. *See, e.g.*, Texas Tax Code Chapter 112. Therefore, Comptroller Hegar acts outside of his authority when he imposes Texas sales and use tax in violation of this governing law and judicial interpretations of that law.

146. Here, Comptroller Hegar acted *ultra vires* by assessing Texas sales and use tax on Pointsmith's fulfillment services when they are not taxable under Texas Tax Code Chapter 151. He then compounded that error by continuing to assert the validity of his assessment notwithstanding the trial judge's interpretation of the governing law and judgment in Pointsmith's favor ruling that its fulfillment service was not subject to Texas sales and use tax.

147. Therefore, Comptroller Hegar acted *ultra vires* by misinterpreting the limitations on his taxing authority and/or acting without reference to or in conflict with the law enabling him to act. *Hall v. McRaven*, 508 S.W.3d 232, 240-242 (Tex. 2017) citing *Houston Belt & Terminal Ry. Co. v. City of Houston*, 487 S.W.3d 154 (Tex. 2016); *Cobb v. Harrington*, 190 S.W.2d 709 (Tex. 1945) (affirming declaratory relief that the taxpayer was not engaged in a taxable activity under the statute and, therefore, was not liable for the occupations tax assessed by the Comptroller).

148. Therefore, Pointsmith seeks the following declarations:

- a. Fulfillment services are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- b. The charges for leasing storage space for customers to store tangible personal property – a component of Pointsmith's fulfillment service – are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- c. The charges for handling (picking customer-selected items from the customer's leased storage space, packing them into boxes, and sealing the boxes) – a component of Pointsmith's fulfillment service – are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.

- d. The charges for shipment of customers' boxed items – a component of Pointsmith's fulfillment service – are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- e. Pointsmith's fulfillment services are not taxable under Texas Tax Code §§ 151.051, 151.010 and 151.0101.
- f. None of the individual components of Pointsmith's fulfillment service constitute "a part of the sale" of a taxable item under Texas Tax Code § 151.051, 151.010 and 151.0101.
- g. Pointsmith's fulfillment service is not a service that is "a part of the sale" of a taxable item under Texas Tax Code § 151.007.
- h. None of the individual components of Pointsmith's fulfillment service are "a part of the sale" of a taxable item under Texas Tax Code § 151.007.
- i. Pointsmith's sale of custom printed materials and its provision of fulfillment services are distinct and identifiable.
- j. Pointsmith's sale of custom printed materials and its provision of fulfillment services are readily separable.
- k. Pointsmith's sale of custom printed materials and its provision of fulfillment services are independently desired.
- l. Pointsmith's sale of custom printed materials and its provision of fulfillment services are independently provided.

- m. In endeavoring to compel Pointsmith to pay Texas sales and use tax on its fulfillment service in violation of Texas Tax Code Chapter 151, the Comptroller is acting wrongfully and without legal authority.
- n. In endeavoring to compel Pointsmith to pay Texas sales and use tax on its fulfillment service in violation of a prior Travis County District Court judgment, the Comptroller is acting wrongfully and without legal authority.

149. The need for declaratory relief, in addition to that provided by Pointsmith's protest suit, is evidenced by the Comptroller's refusal to follow the district court judgment and to apply it to Pointsmith's subsequent periods.

IX. The Doctrines of Res Judicata and Collateral Estoppel Prohibit the Re-Litigation of Previously-Decided Claims and Issues and Require Judgment in Pointsmith's Favor.

150. Under the doctrines of res judicata and collateral estoppel, the Comptroller should be prohibited from re-litigating claims and issues previously decided through the protest suit for the 2003-2007 audit period.

151. As to res judicata, there is a final judgment on the merits by a court of competent jurisdiction between the very parties to this suit based upon claims actually litigated in or should have been litigated in the prior protest suit for an earlier audit period.

152. As for collateral estoppel, the facts sought to be litigated in the present action were fully and fairly litigated in the prior protest suit for an earlier audit period, those facts were essential to the judgment in the prior protest suit, and the same parties were cast as adversaries in the first action.

153. Therefore, the Comptroller should be prohibited from re-litigating claims and issues previously decided and judgment should be rendered in Pointsmith's favor.

X. The Comptroller Abused His Discretion by Failing to Waive All Penalty and Interest Assessed

154. The Comptroller has discretionary authority to waive penalties and interest if a taxpayer exercised reasonable diligence to comply with the tax laws. See Tex. Tax Code § 111.103; 34 Tex. Admin. Code § 3.5.

155. Pointsmith exercised reasonable diligence to comply with the tax laws and cooperated throughout the audit process.

156. Therefore, the Comptroller failed to exercise his discretion to abate all penalty and interest assessed

XI. The Actions of Comptroller Hegar and His Office Warrant Sanctions.

157. The Comptroller's decisions to ignore the Travis County District Court judgment treating Pointsmith's fulfillment service as non-taxable and continuing to assert his that Pointsmith owes additional Texas sales and use tax per his assessment warrant sanctions to stop the harm caused by the Comptroller in forcing Pointsmith to defend against his baseless action.

158. In light of the judgment rendered on a dispute arising between these same two parties on the same legal issue, the Comptroller's tax assessment is groundless and frivolous. The Comptroller's continued assertion of his claim that Pointsmith owes additional Texas sales and use tax is for the purpose of harassment and to force Pointsmith to incur litigation costs so that Pointsmith will relent and pay tax that is not due. The Comptroller's actions constitute bad faith. *See, e.g., Bullock v. Sage Energy Company*, 728 S.W.2d 465 (Tex. App.—Austin 1987, writ ref'd n.r.e.) (wherein the court of appeals, sua sponte, imposed sanctions when the Comptroller ignored a final judgment of the courts deciding an issue in the taxpayer's favor).

159. Therefore, Pointsmith moves for the full scope of relief afforded by Texas Civil Practice and Remedies Code Chapter 10 and Texas Rule of Civil Procedure 13.

160. For example, Pointsmith seeks to recover against the Comptroller and his attorneys (1) attorney's fees incurred to litigate this protest suit, (2) sanctions to compensate for expenses incurred due to Comptroller misconduct (*e.g.*, CPA and attorney's fees and lost employee productivity), and (3) death penalty sanctions, including but not limited to an order instructing the Comptroller to reduce the assessment to \$0 and/or to return Pointsmith's protest payment.

161. Pointsmith also seeks relief under Civil Practice and Remedies Code Chapter 105, the purpose of which is to afford an aggrieved citizen some remedy from a governmental agency for the misuse of governmental power. *Black v. Dallas County Child Welfare Unit*, 835 S.W.2d 626, 629 (Tex. 1992).

162. A party to a civil suit in a court of this state brought by or against a state agency in which the agency asserts a cause of action against the party, either originally or as a counterclaim or cross claim, is entitled to recover, in addition to all other costs allowed by law or rule, fees, expenses, and reasonable attorney's fees incurred by the party in defending the agency's action if: (1) the court finds that the action is frivolous, unreasonable, or without foundation; and (2) the action is dismissed or judgment is awarded to the party. Tex. Civ. Prac. & Rem. Code § 105.002.

163. Under Chapter 105, "cause of action" and "claim" are synonymous. *See* Tex. Civ. Prac. & Rem. Code § 105.003(a) ("To recover under this chapter, the party must file a written motion alleging that the agency's claim is frivolous, unreasonable, or without foundation.

The motion may be filed at any time after the filing of the pleadings in which the agency’s cause of action is alleged.”) (emphasis added); *see also Brainard v. State*, 12 S.W.3d 6, 30 (Tex. 1999) (noting that CPRC Chapter 105 permits attorney’s fees when “a state agency asserts a claim that is frivolous, unreasonable, or without foundation) (emphasis added); *Jaster v. Comet II Const., Inc.*, 438 S.W.3d 556, 564-65 (Tex. 2014) (recognizing the ordinary definitions of both “cause of action” and “claim” to mean facts giving rise to a right that is enforceable in a proceeding).

164. A state agency’s participation in a civil suit as the defendant does not preclude relief under Civil Practice and Remedies Code Chapter 105. *See Brainard v. State*, 12 S.W.3d 6, 30 (Tex. 1999) (addressing plaintiff’s Chapter 105 claim on the merits and not summarily denying the relief because the state agency was the defendant).

165. Here, the operative facts giving rise to the Comptroller’s claim and cause of action arise from his audit of Pointsmith and subsequent assessment of additional Texas sales and use, plus penalty and interest, for which he continues to demand that payment is due.

166. The Comptroller has asserted his claim and cause of action against Pointsmith through both the assessment (*i.e.*, tax bill) sent to Pointsmith and administrative pleadings confirming his demand for the payment of the additional tax, penalty, and interest assessed. *See, e.g., Exhibits 11, 12, and 7 to Exhibit A* (“[The Comptroller] contends the proposed amended audit correctly assesses additional tax based on the facts established by evidence pertaining to the audit period . . .”).

167. Similarly, the Comptroller’s claim and cause of action are asserted through Pointsmith’s Protest Letter and ensuing Original Petition because Pointsmith was statutorily

required to pay “the amount claimed by the state” as a precondition to filing suit under Texas Tax Code Chapter 112 to contest the assessment. *See, e.g.*, Tex. Tax Code §§ 112.051-.052.

168. The Comptroller’s claim and cause of action are frivolous, unreasonable, and/or without foundation because, as detailed above, no material change in law or fact warrants the re-litigation of the taxability dispute previously won by Pointsmith.

169. The totality of the circumstances and evidence demonstrate no arguable basis for the Comptroller’s claim because the trial court has already construed the governing law, applied it to Pointsmith’s facts, and issued a judgment that the Comptroller’s position comports with neither. *See Brainard v. State*, 12 S.W.3d 6, 30 (Tex. 1999); *see also Black v. Dallas Co. Child Welfare Unit*, 835 S.W.2d 626, 629-30 (awarding attorney’s fees where the state agency ignored a prior court orders and continued prosecution of a claim); *State v. Cartwright*, 874 S.W.2d 210, 219-20 (Tex. App.—Houston [14th Dist.] 1994, writ denied) (awarding attorney’s fees where the state agency ignored prior court rulings between the parties).

170. Therefore, under Section 105.003, Pointsmith intends to submit a motion to the court to recover fees, expenses, and reasonable attorney’s fees if the action is dismissed or judgment awarded to Pointsmith.

171. Pointsmith may supplement its motions for sanctions and other relief under Texas Civil Practice and Remedies Code Chapters 10 and 105 and Texas Rule of Civil Procedure 13 with further specific filings. However, Pointsmith now provides the Comptroller with notice of its intent to seek such relief now and we invite the Comptroller to reconsider his assessment against Pointsmith.

PRAYER

WHEREFORE, PREMISES CONSIDERED, Pointsmith respectfully requests that on final hearing:

1. Pointsmith have judgment against Defendants for recovery of \$651,132.64, which represents Pointsmith's estimate of the portion of its \$772,120.45 protest payment attributable to its fulfillment service. However, if the court ultimately determines that the portion of the protest payment attributable to Pointsmith's fulfillment service is higher than \$651,132.64, Pointsmith respectfully prays that it have judgment for recovery of the amount ultimately identified as the sum attributable to this sole contested issue, limited to \$772,120.45, which is the full amount of Pointsmith's protest payment.

2. Pointsmith have judgment against Defendants for statutory interest accrued on its protest payment, as allowed by law.

3. Pointsmith obtain the declaratory relief sought herein under Texas Civil Practice and Remedies Code Chapter 37, Texas Government Code Chapter 2001, and the *ultra vires* doctrine.

4. Alternatively, if the assessment is upheld, waive the assessment of penalties and interest.

5. Pointsmith recover its reasonable costs and attorney's fees.

6. Pointsmith receive such other and further relief to which Plaintiff may be entitled at law or in equity.

REQUEST FOR DISCLOSURE

Defendants are required to disclose, within 50 days of service of this request, the information or material described in Texas Rule of Civil Procedure 194.2.

Respectfully submitted,

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