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Clayton Gray, CGFO, CPM
Chief Financial Officer
City of Sanger
CGray@sangertexas.org

Re: Request for Refund and Residential Use Exemption to Sales Tax Collection by the City of Sanger (the “City”) for the Sale of Electricity to an RV Park owned by Wagon Master RVP Holdings L.L.C. (“Wagon Master”).

Dear Clayton:

Please find below a legal opinion and analysis regarding your questions regarding Wagon Master’s request for refund and exemption to sales tax based on the residential use exemption for purchase of electricity for its RV park.

Short Answer

The City may continue to collect its local 2% sales tax as Sanger is “grandfathered in” regarding the exemption to collection of sales tax for sale of natural gas or electricity, even if Wagon Master may be able to prove that the residential use exemption applies to its purchase. Wagon Master may qualify for the residential use exemption to the State’s portion of the 6.25% sales tax for its purchase of electricity, however, according to 34 Tex. Admin. Code § 3.295, Wagon Master must present a valid exemption certificate showing a predominant or preliminary use study for the request to be accepted in good faith by the City. The City, as the utility, may continue to collect its local 2% and the State 6.25% allocations and let Wagon Master seek its refund from the State until Wagon Master presents a complete exemption certificate that meets the statutory requirements of 34 Tex. Admin. Code § 3.925, or the Comptroller grants a refund.

Analysis

The City may still collect the 2% local tax on sale of electricity to Wagon Master. The residential exemption to sales tax for use of electricity or natural gas applies in municipalities that adopted a local sales tax that was effective after October 1, 1979. *See* Tex. Att’y Gen. Opinion H-1282 (1978). A city that imposed such tax before this date may still levy the tax. 34 Tex. Admin. Code § 3.334(l). The Texas Comptroller maintains an updated list of cities that may still impose a tax on residential use of electricity on its website, and Sanger is listed as a city that, “retained prior to

05/01/79.”¹ This means that even if Wagon Wheel’s use of electricity sold by the City meets the definition of residential use under the Administrative Code, the local tax may still be imposed because the City has effectively been grandfathered in. Therefore, the local 2% may still be collected, despite any presented documentation such as a certificate of exemption from Wagon Master.

Wagon Master may qualify for the residential use exemption to the State’s 6.25% allocation of sales tax collected by the City as the utility. However, the City may still collect this portion, as Wagon Master has not submitted a complete sales and use-tax exemption certificate that meets the statutory requirements under the Administrative Code to qualify for the exemption. Title 34, Section 3.295(a)(8) of the Administrative Code defines residential use as, “use of natural gas or electricity in a building or the portion of a building occupied as a residence and includes:

- (A) Use by the owner of a home, apartment complex, housing complex, condominium, campground, *recreational vehicle park*, nursing home, or retirement home occupied by the owner as a residence;
- (B) Use *by a tenant* in a home, apartment complex, housing complex, condominium, campground, *recreational vehicle park*, nursing home, or retirement home *occupied by the tenant as a residence under a contract for an express initial term of more than 29 consecutive days...*” (emphasis added).

Residential use then could include the electrical use of those tenants staying in Wagon Master’s RV park who stay under a lease for a term of more than 29 days. This could qualify for the residential use exemption as to the State’s portion as there is no “grandfathering” that would apply as it does for the City. However, the Administrative Code provisions for exceptions to sales tax for use of natural gas or electricity provide that a valid exemption certificate, that contains information regarding a predominant use study or projected use study, must be presented to the seller to establish a valid exemption.

The process for a purchaser to claim a refund or exemption for residential use is to first seek that refund or exemption from the seller using an exemption certificate. *Id.* at § 3.325. However, “before a permitted seller refunds to a purchaser tax collected in error on the sale of a taxable item, the permitted seller must obtain from the purchaser a properly completed exemption or resale certificate that meets all the requirements of ... § 3.287 of this title” (relating to Exemption Certificates). *Id.* at § 3.325(b) (emphasis added). Furthermore, “all gross receipts of a seller are presumed subject to sales or use tax unless a valid and properly completed resale or use exemption certificate is accepted by the seller.” *Id.* at § 3.287(d)(1). If the seller accepts a certificate in good faith, then the seller does not then owe the tax to the Comptroller. *Id.* at § 3.287(d)(2). The Administrative Code provides, “an exemption certificate is deemed to be accepted in good faith if...the seller does not know, and does not have reason to know, that the sale is not exempt.” *Id.* at §§ 3.287(d)(2); 3.287(d)(2)(c). In addition, “a permitted seller may assign its right to refund to the purchaser, who may then request a refund directly from the comptroller...” *Id.* at § 3.325(a)(1). In other words, the process laid out in the Administrative Code for refunds or exemptions provides that a purchaser may submit a valid exemption certificate to a seller, and if the seller accepts the certificate in good faith (without

¹ <https://comptroller.texas.gov/taxes/sales/utility/cities.php>

reason to know that the sale is not exempt) then the seller does not owe that tax on the sale of the taxable item and may remit a refund. However, the seller must accept the certificate in good faith and not have reason to know that the sale is not exempt.

Exemption certificates for a purchaser claiming an exemption to sales tax for residential use of natural gas or electricity have additional requirements found in Title 34, Section 3.295 of the Administrative Code. Section 3.295(g)(3) requires, “A natural gas or electric utility study must be completed and on file at the location of the person claiming the exemption at the time an exemption certificate is submitted to the utility company. Without the study, the claim for exemption will be presumed to be invalid.” Those businesses that have existed less than 12 consecutive months may do a projected use study with a registered engineer or person with an engineering degree. § 3.295(g)(2). The utility study, or “predominant use study” is required for, “a Person claiming a sales tax exemption because the predominant use of natural gas or electricity purchased through a single meter is for processing, manufacturing, fabricating, *or another nontaxable use...*” § 3.295(g)(1). A reasonable interpretation of these applicable provisions of the Administrative Code is that *another nontaxable use* includes the residential use exemption, and that a predominant use study or preliminary use study must be submitted by the purchaser in conjunction with the exemption certificate. This interpretation is further supported by Subsection (h)(2) which states,

A natural gas or electricity utility company may only accept an exemption certificate in lieu of tax if the exemption certificate is specific as to the reason for the claimed exemption. For example, if a person is claiming that the predominant use of the utility is for processing, the reason for the exemption must state, ‘A valid and complete study has been performed which shows that (insert the actual exempt percentage) of the natural gas or electricity is for processing tangible personal property for sale in the regular course of business.’

Essentially, there is a strong argument from the Administrative Code that to accept Wagon Wheel’s exemption certificate in good faith, the certificate should provide information about a predominant use study or preliminary study.

Wagon Wheel’s exemption certificate (attached as Exhibit A) claims an exemption from a single meter but does not include information regarding a predominant or preliminary use study. The only reason stated for the exemption is, “151.317(a)(1) Residential used by a RV Park.” Therefore, the City likely has “reason to know” that unless such a study is done, the sale is not exempt. It is important to consider here that if a certificate is accepted without “good faith,” then the City could owe tax back to the Comptroller. Wagon Master has requested both a refund from the City and that the City accept its certificate of exemption. The City could “assign” its right to refund to Wagon Master under Section 3.325, so that Wagon Master could seek its refund request directly from the Comptroller. Since the Administrative Code contains some ambiguity as to the requirement of a predominant use study for the residential use exemption, this would allow the Comptroller to make the determination as to whether the exemption applies to the State’s 6.25% allocation in this circumstance. If the Comptroller were to grant a refund on prior paid State sales taxes, then the City could accept the exemption at that time without the predominant use study in good faith without risking owing taxes back to the Comptroller.

Conclusion:

The City may continue to collect the 2% local sales tax because Sanger is listed as a “grandfathered” City. The 2% may be collected regardless of whether Wagon Wheel’s purchase of electricity falls under the residential use exemption. As to the 6.25% state sales tax, there is doubt as to whether Wagon Wheel’s exemption certification may be accepted in good faith, and the City could deny the certificate based on a presumption of invalidity without a predominant use study. As to the request for refund, if the City assigns its right to refund over to Wagon Wheel as the purchaser, then Wagon Wheel can seek its refund directly from the Comptroller. This method would provide the City with more information going forward.

Please let me know if you have any questions regarding this opinion.

Very truly yours,

/s/ Chace A. Craig

Chace A. Craig

CAC:

cc: Terry Welch, Brown & Hofmeister, LLP