

## **DECISION OF MUNICIPAL TAX HEARING OFFICER**

Decision Date: February 22, 2007

Decision: MTHO #326

Taxpayer: *Taxpayer ABC*

Tax Collector: City of Tucson

Hearing Date: January 22, 2007

### **DISCUSSION**

#### **Introduction**

*Taxpayer ABC* (“Taxpayer”) filed an undated letter of protest of a tax assessment made by the City of Tucson (“City”). After review, the City concluded on October 6, 2006, that the protest was timely and in the proper form. On October 11, 2006, the Municipal Tax Hearing Officer (“Hearing Officer”) ordered the City to file a response to the protest on or before November 27, 2006. On November 6, 2006, the City filed a response. On November 10, 2006, the Hearing Officer ordered the Taxpayer to file any reply on or before December 1, 2006. On November 16, 2006, Taxpayer filed a reply. A Notice of Tax Hearing (“Hearing”) scheduled the matter for hearing commencing on January 22, 2007. Both parties appeared and presented evidence at the January 22, 2007 hearing. On January 24, 2007, the Hearing Officer indicated the record was closed and a written decision would be issued on or before March 12, 2007.

#### **City Position**

The City performed an audit of the Taxpayer for the period June 2002 through May 2006. As a result of the audit, the City assessed Taxpayer for additional taxes in the amount of \$3,921.50, penalties of \$810.34, and interest up through July 31, 2006 in the amount of \$1,324.84. Subsequently, the City waived the penalties. The City asserted Taxpayer was both a retailer and a contractor. The City indicated that under the retail activity, Taxpayer fabricated storage buildings to customer specifications, delivered and set up the buildings on the customer’s property. Under the contracting activity, the City indicated Taxpayer constructed garages for residential customers. The City assessed Taxpayer for additional taxes under the retail activity in the amount of \$11,331.44 which was partially offset by a \$7,409.95 tax credit for the contracting activity.

The City noted the tax on the retail activity resulted primarily from disallowed delivery and warranty deductions claimed by Taxpayer. The delivery deductions were for combined charges for site inspection and delivery of manufactured storage sheds. According to the City, neither the delivery nor the warranty charges were separately invoiced. The City indicated that invoices showed that tax was charged and collected from customers on both these items. The City asserted that City Regulation 19-100.2(a)

("Regulation 100.2") states that "delivery charges" only exist when they are separately charged to the ultimate customer. The City noted that Taxpayer did not sell extended warranty contracts, but instead offered a lifetime warranty included in the price of the storage shed. The City indicated that City Code Section 19-465 ("Section 465") allows for a warranty deduction when it is separately charged for and separately maintained on the books and records. According to the City, Taxpayer's customers had no option on the warranty as it was included in the total selling price of the product.

In response to Taxpayer, the City argued the sale of the storage sheds was not contracting because the sheds were not attached or installed on real property pursuant to City Regulation 415.2(b) ("Regulation 415.2(b)"). The City acknowledged that sheds that were attached to cement slabs would be considered as contracting. The City argued the storage sheds that were not attached to cement slabs would have an "independent functional utility" pursuant to Regulation 415.2(d). Based on the above, the City requested its assessment be upheld.

### **Taxpayer Position**

Taxpayer protested the sale of its storage sheds being considered as retail sales. Taxpayer argued the sale of the sheds should have been classified under the contracting activity. Taxpayer indicated the sheds are customized based on the requirements of each customer. According to Taxpayer, the sheds are custom prepared at Taxpayer's location and trucked to the location of the customer. At that time, the sheds are assembled in the customer's backyard and either secured to a plywood floor or a cement slab. Taxpayer indicated that sometimes the ground must be leveled before the sheds are set up. Taxpayer noted that the Registrar of Contractors considers the fabricating and set up of the sheds as contracting. Taxpayer also constructed garages which were all over 200 square feet in size and all were installed on concrete slabs. Most of the sheds were installed onto plywood floors and were approximately 64 square feet in size. Taxpayer asserted that over fifty percent of the shed costs were for labor.

### **ANALYSIS**

The only issue presented to the Hearing Officer was whether or not the fabrication of customized storage sheds and their delivery and set up at the customer's location would constitute contracting. First, we note that we do not find a Registrar of Contractors license to be dispositive of the issue. The fact that Taxpayer was performing contracting work as a result of constructing garages would require a contractors license. Based on testimony on behalf of Taxpayer, it was clear Taxpayer's storage sheds were built more substantially than a medal storage shed purchased from a home builders supply company. The primary test on whether or not it was contracting is set forth in Regulation 415.2(b) which sets forth the requirement that the sheds would need to be attached or installed on real property in order to be contracting. Regulation 415.2(b) provides further guidance

that the sheds would not be contracting if they had an “independent functional utility”.

Based on the evidence, we conclude the storage sheds with plywood floors were not attached to or installed on real property and would not constitute contracting. We also conclude the storage sheds installed on cement slabs were attached to or installed on real property and would constitute contracting. As to the storage sheds with plywood floors, we conclude based on the size and mobility of the sheds that they would have an “independent functional utility”. Based on all the above, we conclude the sale by Taxpayer of the described storage sheds with plywood floors were properly classified by the City as retail sales. While we recognize this will result in Taxpayer paying City tax on both the materials as well as the substantial labor costs, Taxpayer could have protected themselves by separately itemizing such costs to their customers. For whatever reason, that was not done and as a result Taxpayer must pay City tax on the total selling price. Taxpayer’s protest is hereby denied with the exception of any storage sheds the City may have included as retail sales that were installed on cement slabs. If any of those sales were included as retail sales, the City will need to make an adjustment to the assessment.

#### **FINDINGS OF FACT**

1. Taxpayer filed an undated letter of protest of a tax assessment made by the City.
2. After review, the City concluded on October 6, 2006, that the protest was timely and in the proper form.
3. On October 11, 2006, the Hearing Officer ordered the City to file any response on or before November 27, 2006.
4. The City filed a response to the protest on November 6, 2006.
5. On November 10, 2006, the Hearing Officer ordered the Taxpayer to file a reply on or before December 1, 2006.
6. On November 16, 2006, Taxpayer filed a reply.
7. A Notice scheduled the matter for hearing commencing on January 22, 2007.
8. Both parties appeared and presented evidence at the January 22, 2007 hearing.
9. On January 24, 2007, the Hearing Officer indicated the record was closed and a written decision would be issued on or before March 12, 2007.
10. The City audited the Taxpayer for the period June 2002 through May 2006.
11. The City assessed the Taxpayer for additional taxes in the amount of \$3,921.50, penalties of \$810.34, plus interest up through July 31, 2006 in the amount of

\$1,324.84.

12. Subsequently, the City waived the penalties.
13. The City assessed Taxpayer for retail activities and contracting activities.
14. Taxpayer fabricated storage buildings to customer specifications and delivered and set up the buildings on the property of the customer.
15. The City disallowed delivery and warranty deductions claimed by Taxpayer.
16. Neither the delivery nor the warranty charges were separately charged to the customers.
17. Taxpayer's customers had no option on the warranty as it was included in the total selling price of the product.
18. Some of the sheds were secured to plywood floors.
19. Most of the sheds were secured to plywood floors.
20. For some sheds, Taxpayer had to level the ground before the sheds could be installed.
21. Taxpayer constructed garages which were all over 200 square feet in size and all were installed on concrete slabs.
22. The majority of the shed costs were for labor.
23. Taxpayer had a license from the Registrar of Contractors to perform contracting work.

### **CONCLUSIONS OF LAW**

1. Pursuant to ARS Section 42-6056, the Municipal Tax Hearing Officer is to hear all reviews of petitions for hearing or redetermination under the Model City Tax Code.
2. During the audit period, Taxpayer performed both retail and contracting activities.
3. The storage sheds with plywood floors were not attached or installed on real property.
4. The storage sheds installed on cement slabs were attached to or installed on real

- property.
5. The storage sheds with plywood floors had an “independent functional utility”.
  6. The storage sheds with plywood floors were properly classified by the City as retail sales.
  7. Deductions for labor costs and warranty charges were disallowed because they were not separately charged to Taxpayer customers as required by Section 465 and Regulation 100.2.
  8. Storage sheds installed on cement slabs should have been classified as contracting.
  9. Taxpayer’s protest should be denied with the exception of any storage sheds the City may have included as retail sales that were installed on cement slabs.

### **ORDER**

It is therefore ordered that the protest of *Taxpayer ABC* of a tax assessment made by the City of Tucson is hereby denied with the exception of any storage sheds the City of Tucson may have included as retail sales that were installed on cement slabs.

It is further ordered that the City of Tucson shall revise its assessment for any storage sheds that were included as retail sales that were installed on cement slabs.

It is further ordered that this Decision is effective immediately.

Jerry Rudibaugh  
Municipal Tax Hearing Officer