

05-0973
Audit
Signed 04/19/2006

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER,)	
)	FINDINGS OF FACT, CONCLUSIONS
)	OF LAW, AND FINAL DECISION
Petitioner,)	
)	Appeal No. 05-0973
v.)	
)	Account No. #####
AUDITING DIVISION OF THE)	Audit Period: 12/01/01 – 7/31/04
UTAH STATE TAX COMMISSION,)	Tax Type: Sales and Use Tax
)	
Respondent.)	Judge: Chapman

Presiding:
Palmer DePaulis, Commissioner
Kerry R. Chapman, Administrative Law Judge

Appearances:
For Petitioner: PETITIONER REPRESENTATIVE, Attorney for Petitioner
 PETITIONER, Petitioner
For Respondent: RESPONDENT REPRESENTATIVE 1, Assistant Attorney General
 RESPONDENT REPRESENTATIVE 2, from Auditing Division
 RESPONDENT REPRESENTATIVE 3, from Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing April 4, 2006. Based upon the evidence and testimony presented at the hearing and the post-hearing briefs, the Tax Commission hereby makes its:

FINDINGS OF FACT

1. The tax at issue is sales and use tax.
2. The period at issue is December 1, 2001 through July 31, 2004.
3. PETITIONER, who does business as PETITIONER, is the Petitioner. The Petitioner sells and repairs hot tubs.

4. During the audit period, the Petitioner did not charge and collect sales tax from his customers on amounts charged for labor to repair hot tubs. The Petitioner, however, charged and collected sales tax on the amounts charged for parts required to repair the hot tubs.

5. On June 7, 2005, Auditing Division “(the “Division”) issued a Statutory Notice –Sales and Use Tax (“Statutory Notice”) to the Petitioner, in which it assessed additional sales and use tax for the audit period.

6. The only portion of the assessment in dispute concerns the Division’s imposition of sales tax on the Petitioner’s charges for labor to repair hot tubs.

7. The Division imposed additional tax on charges for repairs of “freestanding” hot tubs, but not on charges for repairs of hot tubs “recessed” either into the ground or into the floor or deck of a building. The Division distinguished between these repairs by having the Petitioner’s bookkeeper segregate the his repair invoices into those relating to freestanding hot tubs and those relating to recessed hot tubs.

8. Prior to the Statutory Notice being issued, the Petitioner and PETITIONER REPRESENTATIVE, his attorney, met with RESPONDENT REPRESENTATIVE 2, a Division Manager, to discuss the Division’s proposed assessment for the audit period. During the meeting, the Petitioner explained that the hot tubs at issue are “hard-wired” into the building’s electrical source, a fact that RESPONDENT REPRESENTATIVE 2 had not known prior to the meeting. Upon learning of this fact, RESPONDENT REPRESENTATIVE 2 verbally told the Petitioner that the hot tubs may be considered real property, upon installation, instead of personal property for sales tax purposes. After the meeting but prior to the issuance of the Statutory Notice, however, RESPONDENT REPRESENTATIVE 2 investigated the issue further and informed the Petitioner in a letter that she had been incorrect and that a freestanding hot tub, whether or not hard-wired, is considered personal property after its installation.

9. Although the Petitioner sells and delivers hot tubs, he is not licensed to connect a hot tub to the real property's electrical power source. Instead, the Petitioner's customer hires an electrician to run metal conduit piping and wiring from the real property's electrical source (either the circuit breaker box or a "sub-box" located nearer the hot tub) and to connect the wiring to four wires located underneath the outside "skirting" of the hot tub. The metal conduit piping may be installed to the property's building or underground, depending upon the placement of the hot tub and the desires of the hot tub owner.

10. The freestanding hot tubs need to be situated on a level surface, such as a concrete pad, decking, or flooring. If located on a deck or a floor, that surface must be reinforced sufficiently to support the weight of the hot tub.

11. The freestanding hot tubs do not require any connection to a water source. All water lines and pumps are located under the skirting of the hot tub.

12. The Petitioner relocates or moves no more than 1% of the hot tubs that he sells and installs. The Petitioner will move a hot tub from one address to another or to another location on the same property for charges that generally range from \$\$\$\$\$ to \$\$\$\$\$ (See invoices in Exhibit R-4). When the Petitioner relocates or moves a hot tub, the customer is required to rent a small crane to assist in the move. Also, an electrician is required to remove the wiring and metal conduit pipe from the hot tub prior to the Petitioner moving the hot tub.

13. When a freestanding hot tub is removed, there is relatively little damage to the real property. However, the concrete pad or the reinforcement added to the decking or flooring, as well as the metal conduit piping and wiring, would remain as part of the underlying real property unless also removed.

14. The Petitioner contends that his services to repair hot tubs, including freestanding hot tubs, are performed on improvements to real property and, as a result, are not subject to sales tax. The Petitioner contends that it his intent for the hot tubs, upon installation, to become part of the underlying realty for their useful lives because they are rarely moved. The Petitioner also argues that the freestanding hot tub become part of the underlying realty upon installation because they are hard-hired into the real property's electrical source and that he will not remove them without an electrician manually severing the electrical connection to the real property and the metal conduit piping. Furthermore, the Petitioner argues that freestanding hot tubs become part of the realty because removal of the hot tubs "scars" the real property as the concrete pad or flooring reinforcements and the metal conduit piping and wiring remain in place.

15. The Division argues that freestanding hot tubs remain personal property after installation and are not permanently attached to the real property, even though they are hard-wired to the real property's electrical source. The Division contends that these hot tubs remain personal property after installation because they are designed to be and are, on occasion, moved from one location to another. The Division further asserts that the hot tubs remain personal property because they are installed on concrete pads, decks, and floors and not recessed into the ground or flooring, thus allowing easy removal with minimal impact to the underlying realty. For these reasons and as evidenced by the invoices it submitted showing that the hot tubs are moved on occasion, the Division asserts that the hot tubs are not permanently attached to real property.

16. The Division also argues that it is long-standing Commission policy that freestanding hot tubs are considered to remain personal property after installation, that they are not considered to be permanently attached to the underlying realty, and as a result, that amounts charged for their repairs are taxable. The Division states that this policy is set forth in Utah State Tax Commission Publication 42

(“Publication 42”), a guideline published by the Commission that is titled “Sales Tax Information for Sales, Installation and Repair of Tangible Personal Property Attached to Real Property.”

18. The Commission revises Publication 42 periodically. Publication 42 (Rev. 6/99) was revised in June 1999 and provides for the taxation of hot tubs on page 14, as follows:

Item	Sale of Item and Repair Parts	Installation Charge	Repair Labor Charges
Hot tub	Treat as personal property taxable to the final customer if portable or free standing. If permanently built into the building or the ground, it is treated as realty taxable to the contractor.	Nontaxable if affixed to a building, deck, patio, gazebo, or ground.	Taxable unless permanently incorporated into the building, such as a tub recessed into the floor.

19. Publication 42 was revised again in April 2002. Publication 42 (rev. 04/02) provides for the taxation of hot tubs on page 7, as follows:

Item	Sale of Items & Repair Parts	Installation Charge	Repair Labor Charges
Hot tub	Treat as personal property taxable to the final customer if portable or freestanding. If permanently built into the building or the ground, it is treated as real property taxable to the contractor.	Nontaxable if affixed to a building, deck, patio, gazebo or ground.	Taxable unless permanently incorporated into the building, such as a tub recessed into the floor.

20. Publication 42 was revised again in December 2005. However, this latest version was revised after the audit period at issue in this matter.

APPLICABLE LAW

1. From December 1, 2001 to July 1, 2002 of the audit period, Utah Code Ann. §59-12-103(1)(g) provided that sales and use tax was imposed on: “(g) amounts paid or charged for services: (i) for repairs or renovations of tangible personal property”

2. Effective July 1, 2002, the Section 59-12-103(1)(g) statutory requirement to tax the repair or renovation of tangible personal property was amended, as follows in pertinent part:

- (g) amounts paid or charged for services:
 - (i) for repairs or renovations of tangible personal property, unless Section 59-12-104 provides for an exemption from sales and use tax for:
 - (A) the tangible personal property; and
 - (B) parts used in the repairs or renovations of the tangible personal property described in Subsection (1)(g)(i)(A), whether or not any parts are actually used in the repairs or renovations of that tangible personal property;

3. The definition of “tangible personal property,” for sales and use tax purposes, was amended during the audit period. Until July 1, 2004, “tangible personal property” was defined in UCA §59-12-102(32) to include “all tangible or corporeal things and substances which are dealt in or capable of being possessed or exchanged” and “all other physically existing articles of things, including property severed from real estate,” but to exclude “real property or any interest or improvements in real estate.” Beginning on July 1, 2004, “tangible personal property” was defined in Subsection 59-12-102(80) to mean, in pertinent part, “personal property that: (i) may be (A) seen; (B) weighed; (C) measured; (D) felt; or (E) touched; or (ii) is in any manner perceptible to the senses.”

4. Utah Admin. Rule R865-19S-78 (“Rule 78”) was adopted to provide guidance concerning the taxation of charges to repair or renovate tangible personal property. The rule in effect during the entirety of the audit period provides as follows in pertinent part:¹

. . . .

¹ Effective June 20, 2005, the Commission amended Rule 78 to provide that “the determination of whether the attachment of an item of tangible personal property to real property suggests that the tangible personal property will remain attached to the real property in the same place over the useful life of the tangible personal property shall be made without regard to the tangible personal property's attachment to a line that supplies water, electricity, gas, telephone, cable, or other similar services.” However, this rule was not in effect during the audit period at issue and has no impact on the Commission’s decision in this matter.

B. Charges for labor to repair, renovate, wash, or clean.

1. Charges for labor to repair, renovate, wash, or clean tangible personal property are subject to sales tax.

....

b) . . . household appliances not permanently attached to a house or building are examples of tangible personal property upon which the sales or use tax applies when repaired. . . .

....

2. Charges for labor to service, repair or renovate real property, improvements, or items of personal property that are attached to real property so as to be considered real property are not subject to sales tax. . . .

a) For purposes of B., fixtures, trade fixtures, equipment, or machinery permanently attached to real property shall be treated as real property while so attached, but shall revert to personal property when severed from the real property.

b) Mere physical attachment is not enough to indicate permanent attachment. Portable or movable items that are attached merely for convenience, stability or for an obvious temporary purpose are considered personal property, even when attached to real property.

c) An item is considered permanently attached if:

(i) attachment is essential to the operation or use of the item and the manner of attachment suggests that the item will remain affixed in the same place over the useful life of the item; or

(ii) removal would cause substantial damage to the item itself or require substantial alteration or repair of the structure to which it is affixed.

....

5. Utah Admin. Rule R865-19S-58 (“Rule 58”) was adopted to provide guidance in differentiating between that tangible personal property that remains tangible personal property after installation to real property and that tangible personal property that becomes an improvement to or part of the real property upon its installation. Rule 58 provides as follows, in pertinent part:

A. Sales of construction materials and other items of tangible personal property to real property contractors and repairmen of real property are generally subject to tax if the contractor or repairman converts the materials or items to real property.

....

2. Fixtures or other items of tangible personal property such as furnaces, built-in air conditioning systems, built-in appliances, or other items that are appurtenant to or incorporated into real property and that become an integral

part of a real property improvement are treated as construction materials for purposes of this rule.

....

D. . . . Examples of items that remain tangible personal property even when attached to real property are:

1. moveable items that are attached to real property merely for stability or for an obvious temporary purpose;
2. manufacturing equipment and machinery and essential accessories appurtenant to the manufacturing equipment and machinery; and
3. items installed for the benefit of the trade or business conducted on the property that are affixed in a manner that facilitates removal without substantial damage to the real property or to the item itself.

DISCUSSION AND CONCLUSIONS OF LAW

At issue is whether the amounts the Petitioner charged to repair freestanding hot tubs during the audit period are taxable or not. Section 59-12-103(1)(g) imposes a sales and use tax on amounts paid or charged for services for repairs of tangible personal property.² Pursuant to Section 59-12-103(1)(g) and the definition of “tangible personal property” provided in Section 59-12-102, the repairs at issue are subject to taxation if the freestanding hot tubs remained tangible personal property after installation, but are not subject to taxation if the hot tubs had become real property or an improvement in real estate after their installation.

Subsection (B)(2) of Rule 78 also provides that repairs are nontaxable if the tangible personal property on which they are made becomes an improvement to or part of the underlying real property after installation. The rule, however, differentiates whether repairs made to tangible personal property that remains tangible personal property after installation are taxable, depending on whether the tangible personal property is “permanently attached” to real property. Section (B)(1) of the rule provides that a repair of tangible personal property that remains tangible personal property after installation is taxable if the tangible personal property is not permanently attached to the real property. Subsection (B)(2)(a), on the other hand, provides that a repair of

² For the latter portion of the audit period, the statute was amended to provide that repairs are not taxable if the tangible personal property upon which the repairs are made is exempt from taxation under UCA §59-12-104. Because hot tubs are not exempt from taxation under Section 59-12-104, the

tangible personal property that remains tangible personal property after installation is not taxable if the tangible personal property is permanently attached to real property.³

In accordance with the statutes and rules in place during the audit period, the repairs of the freestanding hot tubs at issue are taxable if: (1) the hot tubs remain tangible personal property after their installation (i.e., do not become an improvement to or part of the underlying real property); and (2) the hot tubs are *not* permanently attached to the underlying real property. If the Commission determines that either of these circumstances does not exist, the repairs are nontaxable.

The Commission is aware that Publication 42 provides that a hot tub that is not recessed in the ground or floor remains tangible personal property after its installation and is not considered permanently attached to real property for sales tax purposes. The Commission publishes and encourages the use of such guidelines to assist contractors in determining whether they should charge their customers sales tax on their sales and repairs of tangible personal property or not. However, the Commission does not consider the guidelines in Publication 42 to control the outcome in this matter, as would statutory authority or other precedent. Instead, the Commission considers the guidelines to be generalizations that are not binding in an appeal where a decision must be made on the specific facts and circumstances at issue in that appeal. In this appeal, for example, the Commission must determine whether a freestanding hot tub that is “hard-wired” to the real property remains personal property after installation, a factor that is not specifically described in Publication 42.⁴

amendment has no effect in this matter.

3 Effective July 1, 2005, the Legislature codified those portions of the rule that provide that the taxation of a repair of tangible personal property that remains tangible personal property after installation is dependent upon the permanency of its attachment to real property.

4 The Commission notes that in *Chicago Bridge & Iron Co. v. State Tax Comm’n*, 839 P.2d 303(1992), the Utah Supreme Court stated that “[w]hether the subject matter of a sales transaction is deemed real property or tangible property will depend on the facts of each case. The weighing of the

Are freestanding hot tubs personal property or real property after installation? For a portion of the audit period, Section 59-12-102(32) provides that “tangible personal property,” for sales tax purposes, does not include “real property or any interest or improvements in real estate.” Section (A)(2) of Rule 58 provides that “[f]ixtures or other items of tangible personal property such as furnaces, built-in air conditioning systems, built-in appliances, or other items that are appurtenant to or incorporated into real property and that become an integral part of a real property improvement” are considered to become real property or an improvement to real property after their installation. Furthermore, Section (D) of Rule 58 provides a short, nonexclusive list of items that remain tangible personal property after their installation to real property. Although none of three examples in Section (D) is exactly on point, Subsection (D)(3) provides that tangible personal property “affixed in a manner that facilitates removal without substantial damage to the real property or to the item itself” remains tangible personal property after its installation.

The Division explains that it took steps to impose tax only on repairs of hot tubs that were freestanding, not on repairs to hot tubs recessed into the ground or a floor. The Petitioner did not argue that any of additional tax was imposed for repairs on other than freestanding hot tubs. Accordingly, the Commission finds that the repairs at issue were performed on freestanding hot tubs that are located on either a concrete pad or a reinforced floor or deck. Although the hot tubs are “hard-wired” to the underlying real property’s electrical power source⁵ and must be installed on a concrete pad or a reinforced floor or deck, the hot tubs are designed so that they may be moved after installation without damage to the hot tub. A relatively short time is required to disconnect and move a freestanding hot tub from its installed location to another

various factors leading to the ultimate decision by the Commission as to whether a taxpayer is a real property contractor or not is a ruling that is based in part on law and in part on fact.”

⁵ Utah Admin. Rule R865-19S-85(A)(2)(b)(ii) provides that gas, water, electricity, and other supplies lines may be considered “accessories” to tangible personal property. Although this rule addresses “manufacturing machinery and equipment,” it illustrates that the Commission does not necessarily consider

location or a truck for transport. Furthermore, the damage to the real property when a freestanding hot tub is moved appears to be minimal. In fact, the remaining metal conduit piping and concrete pad or reinforcement to the floor or deck could be considered an improvement, not damage, to the underlying real property.

In addition, the Commission is not convinced by the Petitioner's testimony that the hot tubs are "intended" by the parties to become part of the underlying real estate because he moves no more than 1% of the hot tubs he sells and installs. First, there is no evidence to show whether the customers themselves consider the hot tubs to be personal property or part of the real property. Second, the Division has produced invoices from the Petitioner that show that he moves hot tubs from one location to another on occasion. Third, there is no evidence or testimony showing that a freestanding hot tub is generally considered part of the real property when real estate is bought and sold. Lastly, a hot tub need not necessarily be replaced after it removed from a home. Unlike the other types of fixtures listed in Section (A)(2) of Rule 58, a freestanding hot tub is not one that many, if not most, homes have or require. For these reasons, the Commission finds that a freestanding hot tub with the characteristics described by the parties at the Formal Hearing remains tangible personal property after its installation to the underlying real property.

The Commission considers this decision to be consistent with other recent decisions it has issued. For instance, in *Utah State Tax Commission Private Letter Ruling 05-003* (September 27, 2005), the Commission determined that certain playground equipment installed in public parks remained tangible personal property after installation for sales tax purposes. To install the playground equipment, postholes were dug into the ground, the posts holding the playground equipment were placed into the holes, and cement was added to the holes for stability. To move the playground equipment, it needed to be unbolted from the supporting posts, the posts dug out of the ground, the cement broken off the posts, and the holes in the ground

tangible personal property attached to utility supply lines to convert to real property after installation.

filled. Furthermore, the business that sold and installed the playground equipment disclosed that, after the equipment's initial installation, it was only asked to move such equipment two or three times a year.

In *Utah State Tax Commission Private Letter Ruling 04-019* (March 29, 2005) ("PLR 04-019"), the Commission determined that an MRI (magnetic resonance imaging) machine installed in a hospital remained tangible personal property after its installation for sales tax purposes, even though the interior of the hospital required significant modification to support the weight of the MRI. The floor on which the MRI machine was installed required extensive modification to support and provide stabilization, including the addition of horizontal steel beams integrated into the concrete floor and attached to the building's support beams. The MRI machine was then bolted through the concrete flooring to the steel beams. Furthermore, a large hole had to be cut into the outside wall for the MRI to be lifted into place by a crane and the wall then reconstructed after the MRI was installed.

The Commission also considers its decision to be consistent with *Nickerson Pump and Machinery Co. v. State Tax Commission*, 361 P.2d 520 (1961), in which the Utah Supreme Court considered whether large pumps that were sold and then placed into real property remained tangible personal property after installation for sales tax purposes. In finding that the pumps remained tangible personal property, the Court noted that they could be removed without harm to the real property, that they could be moved and used in other locations, and that the placement "was a mere convenience for the purchaser because of the great weight of the pumps which required special equipment to move them."

Are the freestanding hot tubs "permanently attached" to the underlying real property?

Rule 78 provides that tangible personal property is considered permanently attached to real property if:

- (i) attachment is essential to the operation or use of the item and the manner of attachment suggests that the item will remain affixed in the same place over the useful life of the item; or

(ii) removal would cause substantial damage to the item itself or require substantial alteration or repair of the structure to which it is affixed.

Based on the evidence and testimony provided at the Formal Hearing, the Commission considers the attachment of the freestanding hot tubs at issue to the underlying real property to be minimal, given the placement and design of the hot tubs. While some freestanding hot tubs may remain in their original location for their useful life, the manner of attachment is sufficiently minor so that the hot tubs may be moved to another location without extraordinary effort and suggests that they are designed for relocation when so desired.

In addition, the Commission considers that the “damage” to the real property after a freestanding hot tub is removed to be minimal, at most. Furthermore, the damage to a freestanding hot tub that is relocated is inconsequential and, perhaps, nonexistent. For these reasons, the Commission finds that the freestanding hot tubs at issue not only remain tangible personal property after their installation, but that they also are *not* permanently attached to the underlying real property.⁶ Given these conclusions and in accordance with Utah statutes and rules, the Commission finds that the charges for repairs of the freestanding hot tubs at issue are transactions subject to sales tax.

DECISION AND ORDER

Based on the foregoing, the Tax Commission finds that the freestanding hot tubs at issue remain tangible personal property after installation and are not permanently attached to the underlying real property. For these reasons, the Commission finds that the Petitioner’s repairs of the hot tubs are taxable.

⁶ The Division argues that the Petitioner’s treatment of the hot tubs as personal property for purposes of charging sales tax on repair parts was inconsistent with its action of not charging tax on its repairs. However, such action would have been correct had the Commission determined otherwise; that the hot tubs were tangible personal property that were permanently attached to real property.

Appeal No. 05-0973

Accordingly, the Commission sustains the Division's assessment and denies the Petitioner's appeal. It is so ordered.

DATED this _____ day of _____, 2006.

Kerry R. Chapman
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION.

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2006.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Palmer DePaulis
Commissioner

Marc B. Johnson
Commissioner

Notice of Appeal Rights: You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63-46b-13. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. §§59-1-601 and 63-46b-13 et. seq.

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