08-1831
AUDIT- INCOME TAX
SIGNED 03-30-2010

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER. Petitioner, v. AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent.	**INITIAL HEARING ORDER** Appeal No. 08-1831 Account No. ##### Tax Type: Sales and Use Audit Period: 10/01/2004 – 07/30/2007 Judge: Jensen

Presiding:
Clinton Jensen, Administrative Law Judge

Appearances:
For Petitioner: PETITIONER REP., Attorney for Taxpayer
For Respondent: RESPONDENT REP., Assistant Attorney General

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing on December 7, 2009 in accordance with Utah Code Ann. §59-1-502.5.

On July 30, 2008, the Auditing Division of the Utah State Tax Commission (the "Division") issued a Statutory Notice to PETITIONER (the "Taxpayer") for the audit period October 1, 2004 through July 30, 2007. In the Statutory Notice, the Division assessed additional sales and use tax in the amount of $$$$$, plus $$$$$ in interest as of August 28, 2008, for a total assessment of $$$$$.

The Division imposed sales and use tax on countertops that the Taxpayer installed in the homes of end users. The Taxpayer challenges the Division's appeal, claiming that an entity other than the Taxpayer converted the countertops to real property. On that basis, the Taxpayer argues that the other entity would be responsible for any sales tax due for converting personal property to real property.

APPLICABLE LAW

Utah Code Ann. §59-12-103(1)(a) (2007)[1] provides that a tax is imposed on the purchaser for amounts paid or charged for "retail sales of tangible personal property made within the state."

[1] Unless otherwise indicated, the Commission cites 2007 statutes.

Utah Admin. Rule R865-19S-58 ("Rule 58") provides guidance concerning the sale and use tax responsibilities of real property contractors, as follows in pertinent part:

> (1) 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) The sale of real property is not subject to sales tax, nor is the labor performed on real property. For example, the sale of a completed home or building is not subject to the tax, but sales of materials and supplies to contractors for use in building the home or building are taxable transactions as sales to final consumers.
> (a) The contractor or repairman who converts the personal property to real property is the consumer of tangible personal property regardless of the type of contract entered into - whether it is a lump sum, time and material, or a cost-plus contract.
> . . . .
> (3) (c) The contractor must accrue and remit tax on all merchandise bought tax-free and converted to real property. Books and records must be kept to account for both material sold and material consumed.

DISCUSSION

The parties agree that sales tax is due in this case from the person or entity that installs countertops, thus converting the countertops from tangible personal property to real property. Utah courts considering this matter have found that the purchase of tangible personal property to convert it to real property is a taxable transaction as "the last transaction in which those materials can be subjected to sales tax." *See Yeargen, Inc. v. Auditing Division*, 20 P.3d 287, 295 (Utah 2001).

While the parties agree regarding the law to be applied in this case, they disagree regarding the application of the law to the facts of this case. The Division maintains that the Taxpayer purchased materials to fabricate countertops and then incorporated them into real property as a sale of installed countertops.

The Taxpayer maintains that the fabrication and installation of countertops is more properly broken into two separate transactions. The Taxpayer explained that it is a wholesale supplier of countertops. In the transactions at issue, a homeowner contracts with COMPANY A for installed countertops. In a contract that describes the Taxpayer a "Vendor" of COMPANY A, the Taxpayer agrees to fabricate countertops and then install them. The Taxpayer points out that it is in contractual privity with COMPANY A and has no agreement with homeowners.

The Taxpayer admits that it installs countertops in the homes of others and that this action converts the countertops into real property. However, it maintains that it is acting as agent for COMPANY A in

completing the installation because COMPANY A has already purchased the uninstalled countertops in a separate completed wholesale transaction. The Taxpayer argues that this first transaction is complete upon delivery of the finished countertops to the residence in which it will later install them. Under this theory, the Taxpayer argues that the last sale of countertops before their incorporation into real property would be from COMPANY A to the homeowner. In support of this position, the Taxpayer points to its contract with COMPANY A. Specifically, that contract provides as follows under the "Delivery" heading:

> 3. When an Order is designated F.O.B. destination, no liability is incurred by COMPANY A and risk of loss shall not pass to COMPANY A until legal title passes upon receipt of merchandise by COMPANY A at the designated final destination(s) in good condition.

The Taxpayer argues that this provision provides for the passing of title, and therefore the completion of a sale, to COMPANY A upon delivery. The final sale subject to sales tax would then be a sale from COMPANY A to the homeowner.

Reviewing the parties' evidence and arguments, there are two problems with the Taxpayer's argument. The first problem is that the contractual provision on which it relies does not apply unless "an Order is designated F.O.B destination." While it is possible that each of the purchases in the audit is designated "F.O.B. destination," the Taxpayer did not present evidence to demonstrate this. Such a destination would tend to be in conflict with a "Regional Vendor Information" document made a part of the Taxpayer's contract with COMPANY A. In the part of the Regional Vendor Information titled "Freight Terms/F.O.B.," there are three check boxes for "Prepaid – Destination," "Collect – Origin," or "Prepaid/Add – Destination." The parties checked none of the three boxes. Near the bottom of the Regional Vendor Information, the parties have noted "We do not ship – all materials are will call." Additionally, the contract between the Taxpayer and COMPANY A does not specify whether the "destination" is the homeowner's property or whether the countertop is at its "destination" when it is installed in a home.

Even if each of the orders at issue in the Division's audit were "designated F.O.B. destination," there is a second problem with the Taxpayer's position. The provision at issue does not provide for a passing of legal title upon delivery. Rather, it provides that risk of loss shall not pass "until legal title passes upon receipt of the merchandise by COMPANY A at the designated final destination(s) in good condition." This provision falls short of a declaration that passage of title occurs on delivery to the jobsite. At best, the language conditions another event on the passing of legal title. It does not set the terms or otherwise set the time that legal title passes. It does not require that delivery to a homeowner's residence is receipt by

COMPANY A. Nor does it overcome the testimony provided to indicate that the Taxpayer collects one price for installed countertops. On that basis, the transactions at issue are better described as single transactions for installed countertops. In that transaction, the Taxpayer is the entity converting tangible personal property to real property and is the party liable for collecting and remitting sales tax on the transaction.

Although state law rather than a contract between parties determines sales tax obligations, the Commission's decision in this case is consistent with a portion of the contract between the Taxpayer and COMPANY A that specifically deals with tax. That provision, listed under "Miscellaneous Provisions," provides as follows:

> 25. Any and all taxes, fees, imposts, or stamps, required by state, federal, or municipal governments in the selling, transferring, or transmitting of merchandise to COMPANY A shall be paid and assumed by Vendor, including payment of all sums on account of unemployment insurance and other social insurance and old age benefits required by law.

While this language does not control the Commission's decision in this matter, it is noteworthy that the parties' contract, like this Order, finds the Taxpayer the party responsible for any sales tax due for converting personal property to real property.

_____
Clinton Jensen
Administrative Law Judge

DECISION AND ORDER

Based upon the foregoing, the Commission finds that the taxpayer owes Utah sales and use tax on transactions in which it converted tangible personal property into real property in Utah. Accordingly, the Commission sustains the Division's assessment and denies the Taxpayer's appeal. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2010.

R. Bruce Johnson
Commission Chair

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Michael J. Cragun
Commissioner

Notice: If a Formal Hearing is not requested as discussed above, failure to pay the balance resulting from this order within thirty (30) days from the date of this order may result in a late payment penalty.

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