

FINAL PRIVATE LETTER RULING

REQUEST LETTER

10-005

April 12, 2010

VIA HAND DELIVERY

Utah State Tax Commission
c/o Marc B. Johnson
Commissioner
280 North 1950 West
Salt Lake City, UT 84134

Dear Marc,

Pursuant to Rule R861-1A-34, we write to request an **expedited** Private Letter Ruling on a sales tax issue on behalf of our client (“Taxpayer”). This request does not relate to a matter pending before the Commission in an audit assessment, refund request or other agency action, or regarding matters that are pending before a court or judicial review of a Commission decision. We would greatly appreciate a response by April 30, 2010, inasmuch as there is a significant transaction pending that could be delayed absent resolution of this tax issue. We have generally discussed this matter with PERSON, and mutually agreed that a Private Letter Ruling would be appropriate.

Applicable Legal Standards

Section 59-12-104(13) of the Utah Code Annotated is known as the “isolated and occasional” sales and use tax exemption. It provides an exemption from the sales tax for sales of personal property by a person “not regularly engaged in the business of selling that type of tangible personal property.” Section 104(13)(c) authorizes the Tax Commission to “make rules establishing the circumstances under which” this exemption applies.

Administrative Rule R865-19S-38 sets forth certain nonexclusive examples of when the isolated and occasional sales and use tax exemption is applicable. Subsection (2) of this Rule prescribes that “sales made by officers of a court, pursuant to court orders, qualify for the isolated or occasional sales and use tax exemption.”

Ruling Sought

We seek a ruling that the isolated and occasional exemption applies to the transaction described below in which personal property formerly owned by a debtor is transferred to a lender in connection with a deed in lieu of foreclosure.

Facts

Taxpayer is a financial institution. Taxpayer loaned funds to a real estate investment trust (“REIT”). The loan is secured by real and personal property in the State of Utah owned by REIT, including land, a hotel on the land, and personal property inside the hotel (collectively, the “Hotel”). REIT leases the Hotel to an entity related to the REIT. The related entity operates the Hotel.

REIT is delinquent in making payments to Taxpayer on the loan. Pursuant to the terms of the loan documents, Taxpayer has the right to seek a foreclosure on the Hotel. Instead of pursuing formal foreclosure proceedings, Taxpayer and REIT have tentatively agreed to avoid the foreclosure process in order to reduce costs, expedite the transfer, and facilitate a more orderly transfer of the Hotel. Accordingly, REIT will deliver a deed in lieu of foreclosure to Taxpayer. In connection with the deed in lieu, REIT will transfer all of the personal property in the Hotel.

Taxpayer would prefer to receive timely loan payments from REIT, rather than owning the Hotel and personal property. Taxpayer and REIT have not devised this transaction in order to transfer the personal property and avoid sales tax. Taxpayer is not regularly engaged in selling the type of personal property located in the Hotel.

Discussion

The Transfer Here in Connection with a Deed In Lieu of Foreclosure Should Be Exempt From Sales Tax, Because A Transfer under Threat of Foreclosure is Essentially Equivalent to Foreclosure

The Commission has sensibly promulgated a rule that qualifies foreclosures as isolated and occasional sales. A foreclosure is not a retail sale as contemplated by the Sales Tax Act, but is an isolated and occasional act. Rule R865-19S-38(2)(c). This rule should be read to include a transfer made under threat of foreclosure. Otherwise, the Commission’s rule would create a large incentive to increase the number of foreclosures in the state, instead of allowing parties to settle matters in the most efficient manner (without having to resort to full, formal proceedings). Multiplying formal foreclosure proceedings would increase the burden on the courts as well as on lending institutions and the financially distressed parties that find themselves facing foreclosure.

Black's Law Dictionary defines a "deed in lieu of foreclosure" as a "substitute for foreclosure":

A deed by which a borrower conveys fee simple title to a lender in satisfaction of a mortgage debt and as a substitute for foreclosure.

Black's Law Dictionary (8th Ed. 2004). Accordingly the deed in lieu should be treated the same as a transfer by foreclosure.

The Utah Attorney General's Office considered a similar issue – whether sales tax applied when the Small Business Administration conducted a non-judicial foreclosure liquidation. See Opinion of the Office of the Attorney General of the State of Utah No. 78-203 (attached). As set forth in the opinion, the Administrative Rule regarding isolated and occasional sales in force at the time of this opinion was nearly identical to the Administrative Rule now in force with respect to matters relating to foreclosure.

The Attorney General's Office concluded that "non-judicial foreclosure sales of fixed assets by the S.B.A. would be exempt from sales or use taxation" in part because "it would not be correct to say that the S.B.A. was in the 'business' of foreclosure and liquidation." *Id.* The same is true here, as the Taxpayer, a financial institution, is not in the business of foreclosing on hotels and acquiring their personal property.

If you have any questions regarding the foregoing, or need additional information, please do not hesitate to contact me at PHONE.

Very truly yours,

COMPANY

NAME

INITIALS/sal
Enclosure

RESPONSE LETTER

May 6, 2010

NAME
COMPANY
ADDRESS

RE: Private Letter Ruling Request–Sales Tax Treatment of Transfer of Hotel Property by a REIT to a Lender in Connection with a Deed in Lieu of Foreclosure

Dear NAME:

You have requested a ruling on behalf of your client (“Taxpayer”) about whether a transfer of personal property in connection with a deed in lieu of foreclosure is exempt from sales tax. You explained:

Taxpayer is a financial institution. Taxpayer loaned funds to a real estate investment trust (“REIT”). The loan is secured by real and personal property in the State of Utah owned by REIT, including land, a hotel on the land, and personal property inside the hotel (collectively, the “Hotel”). REIT leases the Hotel to an entity related to the REIT. The related entity operates the Hotel.

REIT is delinquent in making payments to Taxpayer on the loan. Pursuant to the terms of the loan documents, Taxpayer has the right to seek a foreclosure on the Hotel. Instead of pursuing formal foreclosure proceedings, Taxpayer and REIT have tentatively agreed to avoid the foreclosure process in order to reduce costs, expedite the transfer, and facilitate a more orderly transfer of the Hotel. Accordingly, REIT will deliver a deed in lieu of foreclosure to Taxpayer. In connection with the deed in lieu, REIT will transfer all of the personal property in the Hotel.

Taxpayer would prefer to receive timely loan payments from REIT, rather than owning the Hotel and personal property. Taxpayer and REIT have not devised this transaction in order to transfer the personal property and avoid sales tax. Taxpayer is not regularly engaged in selling the type of personal property located in the Hotel.

You have argued that the transfer to the Taxpayer is similar to an exempt foreclosure sale made by officers of a court pursuant to a court order, as provided in R865-19S-38(2)(a) and (2)(c). You have also argued that the Commission should follow Opinion 78-203 by the Utah Attorney General’s Office, a copy of which you provided.

I. Applicable Law

Utah Code § 59-12-103(1)-(1)(b)(ii) states:

- (1) A tax is imposed on the purchaser . . . for . . .
 - (a) retail sales of tangible personal property made within the state . . .

Utah Code § 59-12-104(13) provides the following exemption for certain sales of tangible personal property:

- (a) except as provided in Subsection (13)(b), the sale of tangible personal property or a product transferred electronically by a person:
 - (i) regardless of the number of transactions involving the sale of that tangible personal property or product transferred electronically by that person; and
 - (ii) not regularly engaged in the business of selling that type of tangible personal property or product transferred electronically;
- (b) this Subsection (13) does not apply if:
 - (i) the sale is one of a series of sales of a character to indicate that the person is regularly engaged in the business of selling that type of tangible personal property or product transferred electronically;
 - (ii) the person holds that person out as regularly engaged in the business of selling that type of tangible personal property or product transferred electronically;
 - (iii) the person sells an item of tangible personal property or product transferred electronically that the person purchased as a sale that is exempt under Subsection (25); or

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Utah Admin Code R865-19S-38 provides additional guidance on the above exemption, stating in part:

- (1) “Isolated or occasional sales and use tax exemption” means a sale that qualifies for the sales and use tax exemption for the sale of tangible personal property by a person:
 - (a) regardless of the number of sales of that tangible personal property by that person; and
 - (b) not regularly engaged in the business of selling that type of property.
- (2) (a) Except as provided in Subsection (2)(b), sales made by officers of a court, pursuant to court orders, qualify for the isolated or occasional sales and use tax exemption.
 - (b) Sales made by trustees, receivers, or assignees in connection with the liquidation or conduct of a regularly established place of business do not qualify for the isolated or occasional sales and use tax exemption.
 - (c) Examples of sales made by officers of a court pursuant to court order, that qualify for the isolated or occasional sales and use tax exemption are

sales made by sheriffs in foreclosing proceedings and sales of confiscated property.

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- (5) Sales that qualify for the isolated or occasional sales and use tax exemption include sales that occur as part of:
 - (a) the reorganization, sale, or liquidation of a business so long as those sales do not include items purchased exempt from sales tax as a sale for resale;
 -
 - (c) the sale of business assets that are:
 - (i) not purchased sales tax exempt by the business as a sale for resale; and
 - (ii) a type of property not regularly sold by the business.
 - (6) An example of a sale that qualifies for the sales and use tax exemption under Subsection (5)(a) is a sale, even if it is one of a series of sales, to liquidate the fixtures and equipment of a manufacturing company.
 - (7) Examples of sales that qualify for the sales and use tax exemption under Subsection (5)(c) include the sale by a:
 - (a) grocery store of its cash registers, shelves, and fixtures;
 - (b) law firm of its furniture; and
 - (c) manufacturer of its used manufacturing equipment.
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II. Analysis

The transaction you have described is exempt under § 59-12-104(13)(a). The REIT is transferring the hotel tangible personal property, and it is “not regularly engaged in the business of selling that type of tangible personal property.” Furthermore, the exceptions of § 59-12-104(13)(b) have not been met: no facts suggest that the REIT is regularly engaged in selling hotel property or that the REIT holds itself out as a seller of hotel property or that the REIT purchased the tangible personal property tax-exempt under the resale exemption found in § 59-12-104(25).

Moreover, under R865-19S-38 the transfer of the hotel property by the REIT would qualify as an exempt sale under Subsections (5)(a) and (5)(c). For Subsection (5)(a), the REIT is transferring the business associated with the hotel property and no item of that property was purchased tax-exempt under the resale exemption. For Subsection (5)(c), the REIT is transferring property that was not purchased tax-exempt and is not of a type regularly sold by the REIT. Thus, the REIT’s transfer of the hotel property to the Taxpayer is a situation similar to the tax-exempt examples provided in R865-19S-38, Subsections (6) and (7).

III. Conclusion

For the situation you described, the Commission finds that the REIT’s transfer of personal property to the Taxpayer is exempt from sales tax under § 59-12-104(13)(a). This ruling is based on current law and could be changed by subsequent legislative action or judicial

interpretation. Also, our conclusions are based on the facts as described. Should the facts be different, a different conclusion may be warranted. If you feel we have misunderstood the facts as you have presented them, you have additional facts that may be relevant, or you have any other questions, you are welcome to contact the Commission.

For the Commission,

Marc B. Johnson
Commissioner

MBJ/aln
10-005