SUPREME COURT, STATE OF COLORADO

CASE NO. 89SC361

BRIEF OF THE COLORADO MUNICIPAL LEAGUE AS AMICUS CURIAE

THE CITY OF COLORADO SPRINGS; J.H.B. WILSON, Director of Finance for the City of Colorado Springs,

Petitioner,

v.

INVESTMENT HOTEL PROPERTIES, LTD.,

Respondent

CERTIORARI TO THE COLORADO COURT OF APPEALS
(Case No. 88CA0304)

Division II
Opinion by Judge Smith, Dubofsky and Silverstein, J.J., concur

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I. Issue Presented for Review

Whether the Court of Appeals erred in determining that the purchase of tangible personal property for use in a hotel's guest rooms is considered a wholesale sale under the City's sales and use tax code and thus exempt from taxation.

II. Statement of the Case

The League hereby adopts and fully incorporates by reference the statement of the case in the opening brief submitted by petitioner, the City of Colorado Springs.

III. Statement of Facts

The League hereby adopts and fully incorporates by reference the statement of facts in the opening brief submitted by the Petitioner, the City of Colorado Springs.

IV. SUMMARY OF ARGUMENT

In this case the Court of Appeals focused entirely upon whether the Hotel's purchase of guest room furnishings might, under the various definitions found in the City's sales and use tax code, be characterized as a sale for "taxable resale." The Court completely ignored the requirement in the City's wholesale sales exemption that the Hotel demonstrate that its purchase of

guest room furnishings was not for its own consumption, use, storage or distribution. In so doing the Court of Appeals failed to strictly construe the City's wholesale sales exemption in favor of the City and against exemption in favor of the City, failed to read the ordinance, as a whole, and failed to give effect to all provisions of the ordinance as required by well established rules of this Court. The Hotel's purchase of guest room furnishings was for the Hotel's own use in providing lodging services; thus, its purchase of such tangible personal property was not a tax-exempt wholesale purchase under the City's wholesale sales exemption.

The City's Director of Finance correctly determined that the Hotel's purchases were for its own use, and the Court of Appeals erred in overturning the Director of Finance's decision in this C.R.C.P. Rule 106 (a)(4) proceeding. The Court of Appeals cited no authority whatsoever, either from Colorado or any other jurisdiction, to support its conclusion in this case; the Court of Appeals decision is inconsistent with decisions of this Court, the Colorado Court of Appeals and courts from across the country. The decision of the Court of Appeals in this case should be reversed, and the decision of the City's Director of Finance and the El Paso County District Court reinstated.

V. INTRODUCTION

The League is a non-profit voluntary association of 244

municipalities located throughout the state of Colorado, including all home rule municipalities, all municipalities greater than 2,000 in population, and the vast majority of those having a population of 2,000 or less.

195 Colorado municipalities have enacted sales tax ordinances in order to generate revenue for provision of municipal services to their citizens. Colorado municipalities derive an average of 58.2 percent of their annual tax revenue from sales tax, far above the national average of only 17 percent. The sales tax ordinances of many Colorado home rule municipalities, and the Colorado sales tax statutes (which define the sales tax base and exemptions for statutory municipalities) contain language very similar to that construed by the Court of Appeals in the present case. If permitted to stand, the Court of Appeals' decision in the case at bar could have a profound and adverse impact on municipal sales tax collections statewide.

For example, many sales tax codes of home rule municipalities contain language defining "sale" as including rentals of tangible personal property or expressly including furnishing of accommodations. Additionally, many home rule municipalities' sales and use tax codes contain wholesale sales exemptions similar to the Colorado Springs exemption applied in this case, except that most such exemptions are broader in that they exempt purchases for "resale," whereas Colorado Springs

exempts only purchases for "taxable resale."

In this context the Court of Appeals' decision, if permitted to stand, would doubtless result in municipalities being obliged to respond to a flood of litigation by taxpayers seeking to utilize the Court of Appeals' expansive interpretation in this case of the wholesale sales exemption.

Owners of theaters would argue that their seating is purchased at wholesale because it is for "resale" (rental) to theater patrons. Golf course operators will claim that purchases of greens and sod for is "resale" (rental) to persons who pay to use their golf courses. Bowling alley, arcade and amusement park operators will claim that (since after the Court of Appeals decision their <u>own</u> use of equipment can be ignored) equipment is purchased for "resale" to their customers. In some jurisdictions, restauranteurs will argue that their dining charges include a "license to use" (thus, "sale") of the dining room equipment and furniture to patrons. The Court of Appeals unnecessarily invited these and other arguments when it rendered its unfortunate decision dramatically expanding the potential reach of wholesale sales exemptions.

IV. ARGUMENT

A. The Court of Appeals failed to strictly construe the City's

wholesale sales exemption in favor of the City and against exemption, failed to read the ordinance as a whole, and failed to give effect to all provisions of the ordinance.

In this case Division II of the Court of Appeals reversed a decision of the El Paso County District Court, and held that I.H.P.'s (the Hotel's) purchase of guest room furnishings was a wholesale, and thus tax-exempt, transaction under the City of Colorado Springs' (the City's) sales and use tax code.

The wholesale sales exemption in the City's code (Section 7-2-442) provides:

> The sale by wholesalers or retailers to a licensed retailer, jobber, dealer or other wholesaler for purposes of taxable resale, and not for the retailer's, jobber's, dealer's or wholesaler's own consumption, use, storage or distribution, shall be deemed to be wholesale sales and exempt from taxation.

Thus, for a sale to be tax-exempt under the City's wholesale sales exemption, that sale must be: (a) "for purposes of taxable resale" by the purchaser *and* (b) <u>not</u> for the purchaser's "own consumption, use, storage or distribution."

The Court of Appeals focused on the City's tax code definition of "retail sale" and the fact that the City imposes a

tax on hotel room charges to reach its conclusion that the Hotel's purchase of guest room furnishings was for "taxable resale." At this point the Court of Appeals terminated its analysis, declared the transaction wholesale, and decided against the taxing authority and in favor of exemption for the Hotel.

The Court of Appeals treated its conclusion on what ought to have been an intermediate question, viz: was this a sale for "taxable resale," as determinative of the ultimate question of whether the sale of guest room furnishings was a wholesale sale. In so doing, the Court of Appeals read out of the City's wholesale sales exemption a portion of its express language.

It is well settled that a statute should not be interpreted so as to render one of its parts inoperative, In re Coleman American Companies, Inc. 6 BR 251 (Colo. 1980); effect should be given to every provision of a statute. Parker v. US, 448 F.2d 793 (10th Cir. 1971); Colorado General Assembly v. Lamm, 700 P.2d 508 (Colo. 1985). See also: 2A Singer, *Sutherland Statutory Construction*, Sec. 46.06 (4th ed.). This Court has long held that a statute, and separate clauses therein, must be read and considered as a whole. See: Sargent School District v. Western Services, Inc., 751 P.2d 56 (Colo. 1988); People v. District Court, 713 P.2d 918 (Colo. 1986); Clark v. Fellin, 251 P.2d 940 (Colo. 1953); Woodmen of the World v. McCue, 294 P. 947 (Colo. 1931); Dekelt v. People, 99 P. 330 (Colo. 1909).

The effect of the Court of Appeals decision is to simply treat all sales, which may be to some extent for taxable resale, as wholesale sales. This was clearly not the legislative intent behind the wholesale sales exemption, since the City COuncil chose to include the limiting language "and not for the [purchaser's] own consumption, use, storage and distribution" in the exemption.

Additionally, in its sales and use tax code (at Section 7-2-104), the City defines "retail sale" as:

> Any sale, purchase, lease, rental or grant of license to use tangible personal property, or taxable services within the City *except* a wholesale sale *or* purchase for taxable resale (emphasis added).

The Court of Appeals ignored the fact that the legislative body whose ordinance it was applying had made an express distinction between a "wholesale sale" and a "purchase for taxable resale." This Court has said that, in order to affect legislative intent, statutes which are part of the same code and pertain to the same subject matter must be read in pari materia. Colorado Department of Social Services v. Board of County Commissioners, 697 P.2d 1 (Colo. 1985); Public Employees Retirement v. Greene 580 P.2d 385 (Colo. 1978); In re Organization of Upper Bear Creek Sanitation District, 682 P.2d 61 (Colo. App. 1983); affd., Upper Bear Creek Sanitation District v.

Board of County Commissioners, 715 P.2d 799 (Colo. 1986).

The Court of Appeals decision is inconsistent with the rule that when an exemption from tax is claimed, "the burden is on [the taxpayer] to establish its entitlement thereto and the exemption will be strictly construed in favor of the taxing authority." Regional Transportation District v. Charnes, 660 P.2d 24, 25 (Colo. App. 1989), citing Security Life and Accident v. Heckers, 495 P.2d 225 (Colo. 1972) and Bedford v. Hartman Brothers, Inc., 89 P.2d 584 (Colo. 1938). See also: 68 Am Jur 2d, Sales and Use Taxes, Section 100. "The general rule as to construction of exemptions in tax statutes, as applied to sale tax statutes, is that exemptions are to be strictly construed against the claimed exemption." Annotation: *Construction and Application of Exemption or Deduction Provision of General Sales Tax Act,* 157 A.L.R. 804, 806-807.

The Court of Appeals' analysis failed to even mention the significant "and not for the [purchaser's] own consumption, use, storage or distribution" condition expressly set forth in the City's wholesale sales exemption.

The Hotel is claiming that its purchase of guest room furnishings is an exempt, wholesale transaction. The exemption should be strictly construed in favor of the City, and the Hotel should not be relieved of its clear obligation to establish that

its purchase of guest room furnishings were not for its own consumption, use, storage or distribution.

B. The Hotel's purchase of guest room furnishings were for the Hotel's own use in providing lodging services; such purchases were thus not tax-exempt, wholesale purchases.

The Hotel's purchase of various items of tangible personal property which it uses to furnish its guest rooms is not a wholesale transaction. These were purchases for the Hotel's own consumption and use. The Hotel consumes and uses guest room furnishings in order to successfully further its business purpose, which is to provide marketable lodging service.

The recognition of this fact is derived principally from common sense and ordinary experience. Any attempt by the Hotel to show that it does not use or consume the furnishings which it purchases and decides how to distribute throughout its guest rooms will ultimately collide with reality. There are numerous indicators of this reality, not the least of which was alluded to by the Kentucky Court of Appeals when it confronted a case very similar to the one at bar. In holding that a hotel used guest room furnishings in furtherance of its business purpose, and thus owed tax on the purchase thereof, the Kentucky Court observed that it could not "visualize a hotel which would have the ability or the salesmanship to rent a totally bare room to a prospective guest." Kentucky Board of Tax Appeals v. Brown Hotel Company,

528 S.W. 2d 715 (Ky. App. 1975).

As detailed in the City's brief (City's brief at page 12-14) this is a limited C.R.C.P. Rule 106 (a)(4) review of the decision of the City's Director of Finance in his Final Hearing Determination Notice (Appendix A). In his Final Hearing Determination Notice, the Director of Finance concluded that when the Hotel buys furnishings for its various guest rooms these are not tax-exempt wholesale purchases because, inter alia, "such purchases are for the use by the Hotel in conducting its business in furnishing rooms for rental to its guests" (see Appendix A, page 3; Record V. I., page 68 - 72). The decision of the Director of Finance is correct and is in accord with the conclusion of other courts from across the country which have considered this issue.

In Theo. B. Robertson Products Company v. Nudelman 59 N.E. 2d 655 (Ill. 1945) the Illinois Supreme Court considered a claim by a hotel that it ought not be liable for tax on a purchase of various guest room toiletry items because, the hotel argued, these items were purchased for resale to hotel patrons. The Court said that "[t]he question in this case is whether it can be said that hotels . . . use and consume these articles." Ibid at 656. The Illinois Supreme Court concluded:

> In general contemplation, a given hotel will use so many hundred pounds of tissue, soaps

> and the like. They are the persons who use them in the conduct of their business just as they use furniture or the pictures on the wall, or the rugs on the floor. While no agent or employee of the hotel actually uses or consumes such paper articles and soaps, the use is no less the use by the hotel, for it is generally recognized that such articles are to be furnished by the hotel as the standard method of doing its business just as carpets on the floor and the pictures on the wall are furnished. . . Hotels and office buildings are not in the business of selling paper napkins, tissue, cups, plates and the like, but they are in the business of running a hotel or an office building or the like. We are of the opinion that it is in this sense that they may be said to consume these articles. . . The items here considered are simply a part of the equipment of hotels. Ibid at 657.

In Kentucky Board of Tax Appeals v. Brown Hotel Company, supra, the hotel argued that it should not have to pay use tax on bed linens, draperies, and carpets, etc. purchased for its guest rooms because these items were acquired for "resale" to the hotel's lodging customers. As with the Colorado Springs ordinance, the Kentucky statute defined "sale" as including rentals and other transfers of possession (in lieu of title) of tangible personal property. In holding that the hotel was liable for the tax as the principal user and consumer of the property involved, the Kentucky Court of Appeals said:

> In fact, this personal property is "used" by the hotel in the conduct of its business to make its room livable and rentable. The furnishing of this tangible personal property is a basic prerequisite for the operation of any hotel. Although the guest may be an incidental beneficiary, the prime recipient

> of any benefits arising from its use is the hotel. . . Items of tangible personal property are part of the equipment of the hotel and are incidental to the hotel's operation . . . A hotel, of course, is not a regular vendor to the consuming public of linens, dishes, glasses, silverware, etc., but rather deals almost exclusively in services. The capability of rendering the required service is dependent upon the possession and use of numerous items of tangible personal property such as glassware, silverware, linens, etc. Ibid at 717-718.

In Atlanta Americana Motor Hotel Corp. v. Undercofler, 149 S.E. 2d 691 (Ga. 1966) the Georgia Supreme Court responded to a hotel's "purchased for resale" argument with respect to guest room furnishings (carpet, furniture and television sets, among other items, are mentioned in the opinion, Ibid at 693) and applied a Georgia statute which, like the Colorado Springs ordinance, defined "sale" as including a rental of tangible personal property. The Georgia Supreme Court held that the hotel's rental of its rooms was not a resale of the furnishings therein, and that tax was thus owed on the purchase of such furnishings. The Georgia Court recognized that the property was purchased for the hotel's own use.

> Actually, the [hotel] itself used the property to make its rooms liveable, and thus rentable to guests, and the fact that a part of the charge for the rooms was allegedly attributable to such property does not cause such use to be a resale. Although the plaintiff's guests also used this property while occupying the rooms, they used it as a part of the rooms which they rented, not independently. Not many of them would have cared to use the rooms without any of the items mentioned. Ibid at 695.

The guest room furnishings purchased by the Hotel in the present case are no less for the Hotel's use here than were the furnishings at issue in the cases discussed above for use by the hotels in those cases. Hotels provide lodging service, and they purchase a variety of guest room furnishings to further that business purpose. This was the conclusion of the City's Director of Finance. The decision of the Director of Finance was correct. The Hotel has not carried its burden of demonstrating, in order to prove its entitlement to an exemption from tax, that its purchase of guest room furnishings was not for its "own consumption, use, storage or consumption."

The decision of the Court of Appeals to overturn the determination of the Director of Finance in this C.R.C.P. Rule 106 (a)(4) proceeding was error. The League respectfully urges this Court to reverse the Court of Appeals and uphold the decision of the City's Director of Finance and the El Paso County District Court.

C. The decision of the Court of Appeals is not in accord with Colorado decisions of this and other Colorado Courts.

Having ignored the language in the latter half of the City's wholesale sales exemption, the Court of Appeals compounded its error by losing sight of the intended object of taxation in this case.

After reciting the language of the City's wholesale sales exemption, the Court of Appeals declared that "[t]he question . . . becomes whether the room rental is a taxable sale" (emphasis added) and concluded that, since "sales tax is imposed on the rental of the Hotel's rooms . . . the original purchase must be exempt from tax under the wholesale exemption provision." Opinion at 3. (See Appendix B)

The League respectfully submits that the Court of Appeals proceeded from the wrong question, and this contributed to its unfortunate decision. The question is not whether the room rental is a taxable sale. This case is not about whether the room was purchased for resale. The issue in this case is whether the furnishings in the room were purchased for resale. Thus, the correct question is whether the rental of accommodations by the Hotel constitutes a resale of the various furnishings in the rented room to the Hotel's guests.

The Court was incorrect in concluding that because a tax is imposed on the service of furnishing accommodations, the purchase of property for use by the Hotel in providing that service is purchased for taxable resale. These are separate and distinct transactions involving sales of different items and different objects of taxation.

This Court considered an analogous fact situation in Herbertson v. Cruse, 170 P.2d 531 (Colo. 1946) and reached an opposite result from the Court of Appeals in the case at bar.

Herbertson ran a rental car business, and sought to avoid sales tax on vehicles purchased for his rental fleet by arguing that these were "wholesale" purchases because "he [was] not the ultimate user contemplated by the statute, but the renter [was] the ultimate user." Id. at 533.

This Court rejected Herbertson's claim that his purchases of rental property were wholesale and thus tax exempt.

> We are of the opinion that under the foregoing provisions the sale of an automobile by the wholesaler to the taxpayer in the instant case was a sale by a wholesaler to a user or consumer not for resale, and was therefore subject to a sales tax as a retail sale; that the user and consumer of an automobile may not only be he who devotes it to his own personal use, but also he who, for hire, lends or leases it to a third person. (emphasis added) Id.

As this Court has pointed out, the law concerning wholesale sales is:

> fundamentally intended to impose a tax upon that which is consumed and used and exempts only that which is sold for resale. A controlling factor in the classification [of a sale as wholesale or retail] is the disposition of the goods made by the buyer, and not the character of the business of the seller.

Bedford v. C.F.I. Corp. 81 P.2d 752, 754-755 (Colo. 1938).

Herbertson makes it clear that the purchase of property for use in the conduct of a service business is not a wholesale purchase because the disposition of the goods is use by the buyer in the conduct of his business. The Hotel is in the business of renting accommodations; it purchases and uses guest room furnishings in furtherance of its business purpose.

In Carpenter v. Carman Distributing Company, 144 P.2d 770 (Colo. 1943) taxpayer Carman, a laundry operator, argued that certain laundry repair and packaging materials were purchased at wholesale and should be free of tax. To support his argument that this property was purchased for "resale," Carman cited the fact that the cost of the materials was averaged into the overall price of the laundry service and that the materials became the property of the laundry service customer.

This Court rejected the laundry operator's argument and held the purchases in question subject to tax as retail sales.

> The evidence clearly shows that the laundries and cleaners are engaged in service industries as distinguished from the businesses of resale at retail of tangible items purchased at wholesale for such purpose . . . all these items thus are used, and for all practical purposes consumed by the laundries and cleaners as an incident to, and part of, the service furnished by them. [I]t must be held that these purchases by the laundries were for use and consumption by

them and not for resale. Id. at 744

Like the laundry in Carpenter, the Hotel in this case is engaged in a service industry (lodging), not the business of retailing the various furnishings in its rooms. IHP does not run a furniture or appliance rental shop; IHP runs a hotel.

In Craftsman Painters and Decorators, Inc., et al v. Carpenter, 137 P.2d 414 (Colo. 1943) this Court considered claims by electrical and painting contractors that paint and materials purchased by these contractors were purchased at wholesale and for ultimate resale to the purchaser of the building. The contractors performed their painting and electrical services for a fixed price which included the cost of the materials in question.

This Court stated the question presented in Craftsman as: "were [the contractors] selling to the owner the completed job, or were they selling him separately each pint of paint and each piece of wire used in the job?" Id. at 416. This Court's conclusion was that the contractors:

> purchased the several items of personal property and built them into the structure as an integral part of their entire contract, and then disposed of the completed work to the owner, they were users and consumers and not retailers to the owner of each item, . . . [this conclusion] is absolutely irrefutable on any basis of logical reasoning, and . . .

> authority to support it is no more essential than is authority to support the conclusions that black is not white, or that two plus two equals four. Id.

As in Craftsman, the Hotel here purchases its guest room furnishings for use as part of the service which it sells as a package to its customers. It is this service which the Hotel is in the business of selling; like the painting and electrical contractors in Craftsman, the Hotel is not a retailer to its service customers of each item of guest room furnishings purchased. After all, it is highly unlikely that a hotel guest would be able to obtain a specific reduction in his bill should he have the television, the bed, or other items of guest room furnishings removed from his room.

Perhaps the best guidance for this Court in the present case can be found in A.B. Hirschfeld Press, Inc. v. Denver, XII Brief Times Reporter 1596, ____ P.2d ____ (Colo. 1988) wherein Division III of the Court of Appeals considered whether printer Hirschfeld's purchase of certain "prepress materials" (such as press plates, transparencies, film, color separation, etc.) was a wholesale or retail purchase. The prepress materials were purchased for use in printing a customer's individual order and became the customer's property upon completion of the job. Hirschfeld argued that the prepress materials were purchased at wholesale (tax-free) because the cost of such materials was

included in the final price of the printed items delivered to the customer and the customer received title to the materials.

Citing this Court's decisions in Craftsman Painters and Decorators, Inc. v. Carpenter, supra and Carpenter v. Carman Distributing Company, supra, the Court of Appeals utilized a "primary versus incidental purpose" test in which "the test for taxability is whether the item is purchased primarily for resale or whether its resale is merely incidental to the primary purpose of the later transaction." A.B. Hirschfeld Press, supra, XII Brief Times Reporter at 1597.

Applying this test, the Court observed that "the primary purpose of the printer in acquiring these materials is to produce a final product to be sold to the customer" and that:

> . . . the prepress materials were not acquired by [Hirschfeld] for the primary purpose of reselling them. They were acquired in order to allow [Hirschfeld] to produce a product ordered by its customers. Id. at 1598

Like the printer in Hirschfeld, the Hotel here purchases guest room furnishings so that it can competitively provide its service: short term lodging. The primary purpose of the purchase is so that the Hotel will have something more than a bare, unfurnished room with which to compete for lodging

customers in the marketplace. Transitory use of the furnishings in connection with the rental of lodging by a particular customer (whether this can be characterized as a "resale," or not) is merely incidental to the Hotel's purpose of making its guest rooms marketable. The Hotel's primary purpose for purchasing the furnishings is clearly not to resell them to lodgers (see discussion above at pages 8 - 13). The League submits that it is appropriate for sales tax jurisprudence to recognize the real world distinction between the primary business of a hotel and the primary business of a furniture or appliance rental shop. If anything, the situation is clearer here than it was in Hirschfeld. In Hirschfeld, although the customer received actual title to the prepress materials, this disposition of the property was still "merely incidental" to the service rendered by Hirschfeld. Id. Here the Hotel customer obtains not title, but merely the temporary right to use the Hotel's property incident to his purchase of accommodations.

Division I recognized and applied Hirschfeld's "primary versus incidental purpose" test in Broadmoor Hotel, Inc. v. Charnes, 773 P.2d 627 (Colo. App. 1989), which was decided April 6, 1989, less than a month prior to Division II's decision of the case at bar. Despite the Hirschfeld and Broadmoor decisions, the Court of Appeals in the present case failed to apply or even mention the "primary versus incidental purpose" test when it determined that the Hotel's purchase of guest room furnishings

was wholesale rather than retail. In fact, the Court's opinion is stated in conclusary terms and neither utilizes nor distinguishes any authority from Colorado, or any other jurisdiction, in reaching its decision.

VII. CONCLUSION

The conclusions of the City's Director of Finance in his Final Hearing Determination Notice were correct. Decisions of this Court, the Colorado Court of Appeals and courts in other jurisdictions support the Director of Finance's judgment that the Hotel purchased guest room furnishings for its own use in conducting its business of providing lodging service. The Hotel's purchase of guest room furnishings and its rental of accommodations involve different taxable incidents. This purchase of guest room furnishings was not a purchase for taxable resale. To the extent of any resale of the furnishings can be inferred from the Hotel's provision of lodging service, such resale is merely incidental to the Hotel's primary business purpose. The Hotel's primary business is providing lodging, not renting furniture and appliances.

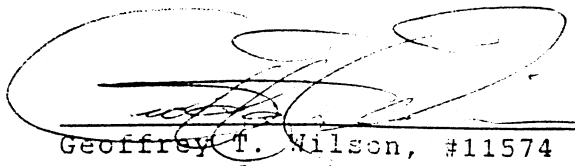
The Court of Appeals erred when it overturned the decision of the City's Director of Finance in this C.R.C.P. Rule 106 (a)(4) proceeding. The Court of Appeals failed to strictly

construe the City's exemption in favor of the City, failed to read the ordinance as a whole, and failed to give effect to all of its parts. The Court of Appeals made a decision contrary to decisions of this Court, the Colorado Court of Appeals and courts from across the country, and cited no authority whatsoever to support its holding.

VIII. REQUEST FOR RELIEF

WHEREFORE, the League respectfully requests this Court to reverse the decision of the Court of Appeals, reinstate the judgement of the El Paso County District Court, and uphold the decision of the City's Director of Finance and the assessment of the City against the Hotel.

Respectfully submitted this 27th day of November, 1989.



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CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the foregoing was mailed, first class postage prepaid, this 27th day of November, 1989, to:

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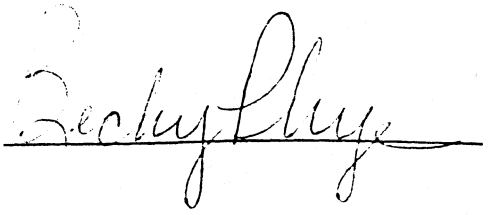

In the matter of the Appeal of INVESTMENT HOTEL PROPERTIES, LTD., Account No. 25635-00-S	)	FINAL HEARING DETERMINATION NOTICE

This matter comes before the Director of Finance pursuant to §7-2-903:H of the Code of the City of Colorado Springs 1980, as amended, a/k/a The City of Colorado Springs Sales and Use Tax Ordinance (hereinafter the "Code") pursuant to an appeal by Investment Hotel Properties, Ltd. ("IHP" or "Taxpayer") from a decision of Larry Allison, City Controller, acting as Referee. This matter has been submitted to the Director of Finance pursuant to a Stipulation of Facts entered into on behalf of the City of Colorado Springs (the "City") by M. Allen Ziegler, Jr., Chief Corporate Attorney for the City of Colorado Springs, and on behalf of IHP by R. Bruce Johnson of Holme Roberts & Owen, attorney for IHP. Both IHP and the City have filed appropriate Briefs with the Director of Finance. The parties have elected to rely upon the Stipulation of Facts agreed to and submitted by the parties. The Director of Finance hereby makes the following Findings of Fact, Conclusions of Law and Final Determination:

FINDINGS OF FACT

1. IHP purchased the Clarion Hotel in Colorado Springs, Colorado, in December 1984 from Denver S.I. Company.

2. The purchase included the transfer of certain items of tangible personal property from Denver S.I. Company to IHP.

3. The original purchase price of the tangible personal property as entered into the accounting records of IHP was $4,138,491.

4. The tangible personal property purchased by IHP included tangible personal property in the lobby, kitchen, restaurant and other common areas of the hotel as well as tangible personal property used exclusively in the guest rooms of the hotel.

5. The City served upon IHP, by certified mail, an assessment of $84,261.06 plus interest of $4,213.05 for a total of $88,474.11 dated February 7, 1986.

6. The purpose of the assessment was to impose the City 2½% use tax of $103,462.28 on the total purchase price of tangible personal property acquired by IHP. A credit was allowed in the computation of the assessment amount for use tax previously paid by the Taxpayer in June, 1985 in the amount of $19,201.22.

7. The Taxpayer entered into an agreement with the City for payment of tax on an installment basis. The payment agreement included additional interest computed at a rate of ½% per month applied to the outstanding principal balance.

8. The Taxpayer subsequently filed a timely protest and request for hearing.

9. An informal hearing was conducted before L.T. Allison, City Controller, on July 10, 1986.

10. During the hearing, the Taxpayer presented evidence that an agreement was reached with Denver S.I. Company, the property's prior owner, which resulted in a reduction of the original purchase price of the Clarion Hotel.

11. The reduction included a decrease of $604,809 allocated to the purchase price paid for the tangible personal property.

12. The City has accepted the Taxpayer's figures, and the taxable purchase price and tax thereon are adjusted accordingly.

13. The adjusted purchase price pertaining to tangible personal property totals $3,533,682 of which $1,833,300 is allocated to the common areas, and $1,700,382 was allocated to the guest rooms. The tax and interest applicable to the total sum are computed to be $88,342.05 and $3,457.04, respectively, for a total of adjusted tax and interest of $91,799.09.

14. The Taxpayer has now paid in its entirety the tax and interest asserted by the City of Colorado Springs pursuant to the assessment and decision of the City Controller of August 26, 1986.

15. The Taxpayer acknowledges that there has been properly assessed use tax pertaining to the purchase of tangible personal property located in common areas of the hotel. However, there is in dispute the portion of use tax and interest pertaining to the purchase of tangible personal property located in guest rooms.

16. The Taxpayer claims a refund of $42,510, plus applicable interest in the amount of $2,125, pertaining to use tax paid to the City on the purchase of tangible personal property used in the guest rooms.

CONCLUSIONS OF LAW

1. The Director of Finance has jurisdiction of this matter pursuant to §7-2-903:H of the Sales Tax Ordinance.

2. The matter to be determined by the Director of Finance is whether the purchases of the items of tangible personal property used in the guest rooms of the taxpayer's hotel are exempt from taxation because the Code imposes a tax upon the rentals of such guest rooms.

3. The Code imposes a sales tax and a use tax at the rate of 2½%. Sections 7-2-103; 7-2-201; 7-2-202 of the Code.

4. The Taxpayer argues that the purchase of the guest room furnishings are exempt from sales and use tax because the furnishings were purchased for the purpose of resale. The Director of Finance rejects this argument.

5. Section 7-2-313 of the Code provides for a tax upon purchase price paid for tangible personal property. The items purchased by the Taxpayer constitute tangible personal property.

6. The City further imposes a tax upon the rental of rooms and accommodations services under §7-2-311 of the Code as follows:

> "The sales or use tax is imposed on the entire price paid or charged on the transaction of furnishing rooms or other accommodations to any person who for a consideration uses, possesses or has the right to use or possess, any room or rooms in any hotel, apartment hotel, guest house, guest ranch, motel, mobile home, auto camp, trailer court or park, under any concession, permit right or access, license to use or other agreement, or otherwise." (emphasis added)

7. For the Taxpayer to qualify for an exemption from the imposition of the taxation upon rooms and accommodation service under §7-2-311 of the Code, the Taxpayer must come within the provisions pertaining to wholesale sales under §7-2-442 of the Code. In other words, the Taxpayer's purchases must be for taxable resale by the hotel to its guests.

8. The Director of Finance concludes such purchases are not for taxable retail sale to the guests. Such purchases are for the use by the hotel in conducting its business in furnishing rooms for rental to its guests.

9. The provisions of §7-2-311 of the Code establishing a sales tax on the rentals of rooms and accommodations are based upon a separate taxable incident, i.e. the rental of such rooms and accommodations and not upon the acquisition of the property located within the rooms.

10. The Director of Finance further notes that the provisions of §7-2-432 of the Code which provide an exemption for room rentals by the month from the imposition of the rental accommodation sales tax is an additional indication that the transactions involving the acquisition of the items to be used in the rooms and the rental of the rooms themselves are separate and distinct transactions.

11. The Taxpayer argues that the provisions in §7-2-421 of the Code pertaining to the exemption from manufactured products, component parts and ingredients are applicable, and thus the furnishings used in the guest room should be exempt from taxation as analogous to this exemption, i.e. the transformation of these items, ingredients or component parts of the hotel room. This argument is rejected as the use of furnishings in the guest room does not constitute a manufacturing operation, and the sales and use tax exemption provisions of the City Code cannot be extended by analogy. See §7-2-401 of the Code.

12. The Taxpayer argues that the imposition of a Sales and Use Tax upon the purchase of the items used in the guest rooms and subsequently a tax upon the rental of the rooms themselves constitutes a pyramiding of taxes. The Director rejects this argument noting that the taxes are based upon separate taxable incidents.

13. The Taxpayer argues that use of the room by the guest constitutes the rental of personal property under §7-2-310 of the Code. This argument is rejected on the basis that the rentals of the room for which the personal property is included is merely one component the separate taxable incident, i.e. the rental of a room.

14. An examination of the cases cited in the City's Brief and the Taxpayer's Brief indicates that cases outside the State of Colorado, with one exception, have considered this issue and have concluded that items purchased for use in guest rooms do not constitute items exempt from either sales or use taxation. Although the Taxpayer disputes the applicability of certain of these cases, the Director finds they are of persuasive value. The Director notes that in Hotel Statler Company, Inc. v. District of Columbia, 199 F.2d 172 (C.A.D.C. 1952) the Court in finding that items were not exempt from taxation concluded in part:

> "Less clearly, perhaps, but nevertheless correctly we think, bed linen, towels, tumblers, light bulks, draperies and carpets do not become parts of the room but are properties used by the hotel in furthering the sales of its room." at 174.

15. In Atlanta Americana Motor Hotel Corporation v. Undercoffer, 149 S.E.2d 691 (Ga. 1966) the Court in denying the Taxpayer's request for a refund, stated:

> "Actually, the Plaintiff itself used the property to make its rooms liveable, and thus rentable to guests, and the fact that a part of the charge for the rooms was allegedly attributable to such property does not cause such use of it to be a resale." at 695.

To the same effect is Kentucky Board of Tax Appeals v. Brown Hotel Company, 528 S.W. 2d 715 (Ky.App.1975). A similar conclusion in regard to the use of air conditioners and television sets in hotel rooms was reached in Commonwealth v. Benjamin Franklin Hotel Company, 28 Pa.D. and C.2d 329 (Pa. 1961).

16. In Tellerant Leasing Corporation v. High, 174 S.E.2d 11 (N.C.App. 1970) the Court, in reaching the same conclusion as the Atlanta Americana case, rejected the argument that there was a double taxation noting that the taxes were on two separate taxable incidents.

17. Finally, in Sine v. State Tax Commission, 15 Utah 2d 214, 390 P.2d 130 (1964) the Court rejected the argument that supplies purchased by a motel came within the manufacturing exemption.

18. The only case presented to the Hearing Officer to the contrary is Hilton Hotels Corporation, d/b/a The Netherlands Hilton Hotel v. Bowers, Ohio Board of Tax Appeals No. 48023 (July 31, 1962) which the Director finds unpersuasive.

Based upon the foregoing Findings of Fact and Conclusions of Law and upon all the proceedings herein, the Director of Finance hereby makes the following final hearing determination:

1. Investment Hotel Properties, Inc. has been appropriately assessed for use tax paid by the Taxpayer for acquisition of items used in the guest rooms and used in the common areas of the hotel.

2. The Taxpayer's request for a refund of $42,510, plus applicable interest in the amount of $2,125, is hereby denied.

Made _____ this 20th day of March, 1987.

J. H. B. WILSON
Director of Finance
City of Colorado Springs

APPROVED AS TO FORM:

FOR THE CITY ATTORNEY
JAMES G. COLVIN II
City Attorney

BY: M. Allen Ziegler
M. ALLEN ZIEGLER, JR.
Chief Corporate Attorney
Attorney for the City of
Colorado Springs

HOLME ROBERTS & OWEN
Attorneys at Law

BY: R. Bruce Johnson
R. BRUCE JOHNSON
Attorney for Investment Hotel
Properties, Ltd.

CERTIFICATE OF MAILING

I hereby certify that I have mailed a true copy of the Final Hearing Determination Notice to R. Bruce Johnson, Esq., Holme Roberts & Owen, Suite 900, 50 S. Main Street, Salt Lake City, Utah 84144, by United States mail, first-class postage paid, on this 20th day of March, 1987.

COLORADO COURT OF APPEALS

No. 88CA0304

INVESTMENT HOTEL PROPERTIES, LTD.,

Plaintiff-Appellant,

v.

THE CITY OF COLORADO SPRINGS, J. H. B. WILSON, Director of Finance for the City of Colorado Springs,

Defendants-Appellees.

Appeal from the District Court of El Paso County
No. 87CV1924

Honorable Douglas E. Anderson, Judge

DIVISION II
Opinion by JUDGE SMITH
Dubofsky and Silverstein,* JJ., concur

JUDGMENT REVERSED AND CAUSE REMANDED WITH DIRECTIONS

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*Sitting by assignment of the Chief Justice under provisions of the Colo. Const., art. VI, Sec. 5(3), and §24-51-1105, C.R.S. (1988 Repl. Vol. 10B).

In this C.R.C.P. 106(a)(4) proceeding, plaintiff Investment Hotel Properties, Ltd. (Hotel), appeals the trial court's judgment affirming the denial of its claim for a sales tax refund. We reverse.

Under Colorado Springs City Code 7-2-313, a sales tax is imposed upon the purchase price paid for tangible personal property. Colorado Springs City Code 7-2-311 further imposes a tax upon the rental of rooms and accommodations.

> "The sales or use tax is imposed on the entire price paid or charged on the transaction of furnishing rooms or other accommodations to any person who for a consideration uses, possesses or has the right to use or possess, any room or rooms in any hotel . . . under any concession, permit right or access, license to use or other agreement, or otherwise." (emphasis added)

The Hotel purchased a hotel in Colorado Springs in 1984. The purchase included the tangible personal property in the guest rooms and common areas. The City of Colorado Springs (City) imposed a sales and use tax on the Hotel's purchase of the personal property. Additionally, the City imposes a rent tax each time a hotel room is rented. The Hotel filed a claim for refund of the sales and use tax paid which claim was denied by the City.

The Hotel then appealed the City's denial to the district court. The district court affirmed, finding that the Hotel was not exempt from taxation for sales and use tax under the wholesale purchase exemption because, although the hotel

guests used the property, it was not a resale of the property.

The Hotel first contends that its purchase of items used to furnish its guest rooms is exempt from tax under the manufacturing exemption contained in the city code. We disagree.

The manufacturing exemption provides that:

> "The purchase price paid or charged on the sales to and purchases of tangible personal property by a person engaged in manufacturing or compounding for use, profit or sale, shall be deemed a wholesale sale when it meets all of the following conditions:
>
> A. It is transformed in fact by the process of manufacture;
>
> B. Becomes by the manufacturing processes a necessary and recognized ingredient, component and constituent part of the finished product; and
>
> C. Its physical presence in the finished product is essential to the use thereof in the hands of the ultimate consumer."

Colorado Springs City Code 7-2-421.

We agree with the trial court that the manufacturing exemption is not applicable because there is no physical transformation pursuant to manufacturing or compounding. See Western Electric Co. v. Weed, 185 Colo. 340, 524 P.2d 1369 (1974).

The Hotel next contends that the trial court erred in determining that a purchase of tangible personal property to be used exclusively in a hotel's guest rooms is not a

wholesale purchase exempt from taxation. We agree with the Hotel that under the wholesale sales provision of the Colorado Springs City Code, the purchases of tangible personal property to be used in the hotel's guest rooms are not subject to tax because such purchases are for taxable resale to the guests.

An exemption from sales tax is provided in the Colorado Springs City Code 7-2-442:

> "The sale by wholesalers or retailers to a licensed retailer, jobber, dealer or other wholesaler for purposes of taxable resale, and not for the retailer's, jobber's, dealer's or wholesaler's own consumption, use, storage or distribution, shall be deemed to be wholesale sales and exempt from taxation."

The question then becomes whether the room rental is a taxable sale. Under Colorado Springs City Code 7-2-104, a retail sale is defined as:

> "Any sale, purchase, lease, rental or grant of license to use tangible personal property, or taxable services within the City except a wholesale sale or purchase for taxable resale."

We conclude that, under the above provisions of the Colorado Springs City Code, the Hotel's rental of its guest rooms constitutes a resale of its tangible personal property. The sales tax is imposed on the rental of the Hotel's rooms, and therefore, the original purchase must be exempt from tax under the wholesale exemption provision.

If, as here, the facts are not disputed, but the law was

erroneously applied to the facts, then the judgment rendered on such facts will not be upheld on review. Maloney v. Denver, 35 Colo. App. 167, 530 P.2d 1004 (1974).

The judgment is reversed and the cause is remanded for further proceedings in accordance with this opinion.

JUDGE DUBOFSKY and JUDGE SILVERSTEIN concur.