

1992

# Valgardson Housing Systems, Inc. v. Utah State Tax Commission : Petition for Rehearing

Utah Court of Appeals

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BRIEF

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DOCKET NO.

920644

IN THE UTAH COURT OF APPEALS

STATE OF UTAH

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VALGARDSON HOUSING SYSTEMS,  
INC.

Petitioner,

vs.

UTAH STATE TAX COMMISSION,

Respondent.

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PETITION FOR REHEARING

Case No. 920644-CA

Priority No. 15

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Petition for Rehearing of Judgment  
of the Utah Court of Appeals

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FILED

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COURT OF APPEALS

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IN THE UTAH COURT OF APPEALS

STATE OF UTAH

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VALGARDSON HOUSING SYSTEMS,  
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Case No. 920644-CA

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PETITION FOR REHEARING

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SUMMARY OF ARGUMENTS

Petitioner, in this Petition for Rehearing, contends that the court granted the Utah State Tax Commission a greater amount of discretion than was intended by the Supreme Court or the legislature. The standard of review in this matter should be a "correction of error" standard rather than the standard used by the court which upholds the decision of the tax commission unless it is "unreasonable or arbitrary".

Petitioner also claims that the distinction made by the State Tax Commission as to the differences between a real property transaction and a personal property transaction does not fit even the standard of reasonableness. Petitioner believes the Utah

Supreme Court has set forth the type of analysis that must be used in such cases; and that neither the Utah State Tax Commission nor this Court has used that standard.

Assuming, but not admitting, that the Court was correct concerning the two points raised above, Petitioner contends that the Court has ordered the wrong transaction taxed. The transaction to be taxed should involve the sale by the contractor-dealer to the ultimate consumer; and this Petitioner should not be liable for any payment or collection of sales taxes.

#### POINT I

IN ITS RULING ON THE STANDARD OF REVIEW, THIS COURT HAS GRANTED THE UTAH STATE TAX COMMISSION GREATER DISCRETION THAN INTENDED BY THE UTAH SUPREME COURT AND THE LEGISLATURE.

The Court, in its opinion in this matter, first stated that this Court would review agency decisions interpreting statutory law by a "correction of error standard" unless the legislature has expressly or impliedly granted the agency discretion to interpret and administer the statute at issue. The Court then found the implied grant of discretion, and changed the standard of review to one that defers to the Tax Commission, unless that decision by the Tax Commission is "unreasonable or arbitrary". In doing so, the court referred to the case of BJ-Titan Services v. State Tax Commission, 842 P.2d 822 (Utah, 1992), where the Utah Supreme Court found "some discretion in determining whether a certain transaction

constitutes a sale of 'tangible personal property'." The Supreme Court again addressed the question in the case of Chicago Bridge & Iron Co. v. State Tax Commission, 839 P.2d 303 (Utah, 1992). The court stated there:

Whether the subject matter of a sales transaction is deemed real property or tangible personal property will depend on the facts of each case. The weighing of the various relevant 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 part on law and part on fact. In ruling on such issues, the Commission must necessarily exercise a degree of discretion, and we accordingly defer to the Commission's determination. We will not upset its ruling unless it is unreasonable or arbitrary. 839 P.2d at 307.

The important part of this statement is the question of "weighing of the various relevant factors leading to the ultimate decision by the Commission as to whether a taxpayer is a real property contractor". This Court has granted carte blanche to the State Tax Commission to decide whether a transaction is a real property or personal property transaction. That is not the authority granted to them by the Utah Supreme Court. In order to be given the deference that they claim, the State Tax Commission must weigh the relevant factors, and must decide whether or not the taxpayer is a real property contractor. As will be seen in Point II herein, the State Tax Commission did not weigh the relevant factors and did not even consider the question as to whether or not the taxpayer is a real property contractor. That was not the

question in the minds of the Tax Commission; and it should have been. Whether the relevant factors were weighed and whether the appropriate law was applied should be decided by a "correction of error" standard as previously suggested by Petitioner. Only after finding that the State Tax Commission went through the appropriate procedure and considered the appropriate factors, must they be granted the discretion referred to by the Utah Supreme Court. There is no question in anyone's mind that Valgardson Housing Systems makes modular buildings which become part of the real estate as soon as they are attached. There is also no question that Petitioner is a licensed general contractor in the state of Utah. Those items have been proved, have been stipulated to, and are not in controversy. The fact that those items were ignored by the Utah State Tax Commission in its decision is a legal error that should be corrected by this Court.

#### POINT II

THE DISTINCTION MADE BY THE STATE TAX COMMISSION BETWEEN A TANGIBLE PERSONAL PROPERTY TRANSACTION AND THAT INVOLVING AN IMPROVEMENT TO REAL ESTATE IS NEITHER CORRECT NOR REASONABLE.

In Point III of its Reply Brief, Petitioner cited the case of Wisconsin Dept. of Revenue v. Sterling Custom Homes Corp., 283 NW.2d 573 (Wis. 1979). That case was almost identical to the present one. The Wisconsin Supreme Court found that the modular



construction company was a contractor, was involved in real estate construction activities, and was entitled to have its activities taxed as improvements to real property. The decision by the Wisconsin Supreme Court goes to the very heart of the matter at issue here. Because the Wisconsin Supreme Court reviewed the same contentions made by the Utah State Tax Commission and refuted them in their entirety, Petitioner asks this Court to review that decision once more. At the risk of being redundant, Petitioner therefore sets forth once again the reasoning of that court.

In a well-reasoned opinion, the Court stated:

In reaching our conclusion that Sterling Homes was a contractor and a consumer of the goods, we look to the general scope of its activities in its home-construction enterprise. 283 N.W.2d at 574.

The facts of the Wisconsin case were almost identical to the present facts:

When the foundation was completed and the builder was ready to erect the house, the taxpayer loaded the components in the sequence that conformed to the order that the components would be used at the job site. The components were delivered to the job site by the taxpayer's trucks and drivers. At the job site, the larger components were unloaded by crane. The crane operators were hired by the builder, but were usually selected by one of the taxpayers' salesmen. . . . Although the drivers' only defined on-site responsibility was to keep a report with respect to the erection, they often helped or supervised, because they were very familiar with the process. 283 N.W.2d at 574-5.

The court went on to say:

The taxability of the transaction transferring the

components to the builder is dependent on whether Sterling Homes was engaged in "real property construction activities." If Sterling Homes was engaged in such an activity, then it is a contractor or a subcontractor and is a consumer of the tangible personal property used in real property construction activities and the sales tax applies to transfers to Sterling Homes and not by it.

The facts demonstrate that, in all respects but one, the taxpayer was engaged in real property construction activities. The lone exception is that Sterling Homes conducted its construction activities at a factory, rather than at the building site. The taxpayer used the materials it purchased for only a single purpose -- to construct custom-designed homes to be assembled at predetermined locations on foundations which were specifically designed for the prefabricated components. The components thus assembled were consumed by the very process of fabrication, for which they would be useless in their fabricated form except for the very building for which designed.

The distinction between on-site and off-site construction of the components is not a criterion upon which the legislature has hinged the question of taxability. Rather, taxability is to be determined by whether or not the taxpayer is engaged in 'real property construction activities.' The record leaves no doubt that Sterling Homes was so engaged. 283 N.W.2d at 575.

It is Petitioner's contention that the Utah Supreme Court has adopted the basic reasoning of the Wisconsin Supreme Court in the Chicago Bridge case, referred to in Point I. In that case, the Utah Supreme Court set forth the kind of analysis to be used to determine questions such as the present one. The Supreme Court stated:

In effect, a real property contractor is treated as a consumer for sales tax purposes.

The reason for this rule is that materials which are

purchased and then converted into real property would escape the sales tax because a sales tax is not imposed on the sale of real property. Real property contractors are therefore considered the consumers because their purchases of materials that are incorporated into real property are the last transactions in which those materials can be subjected to the sales tax.

The test for determining whether a person is a real property contractor is based not only on who converts tangible personal property into real property, but also on the nature of the transaction. 839 P.2d at 306.

A similar line of reasoning was adopted earlier in the case of BJ-Titan Services v. State Tax Commission, 842 P.2d 822 (Utah, 1992). In the BJ-Titan Services case, a cement contractor provided cement to be poured into a well. The court analyzed whether or not the cement became part of the real property, and thus became part of a real property transaction. The court found that it did not. It was admitted by all parties that the well operator was primarily responsible for putting the cement actually into the well. That was not an issue. The only issue was whether or not the cement became part of the realty, and part of a real estate transaction. That is the issue here. Once again, that issue has been ignored. The Chicago Bridge case also quoted the case of Nickerson Pump & Machinery Co. v. State Tax Commission, 361 P.2d 520 (Utah, 1961) which held that a fabricator and installer of large pumps was not a real property contractor. The Chicago Bridge court, referring to its earlier decision, stated:

The Court based that conclusion on several factors: (1)

The pumps were removable without harm to the structures on which they were placed; (2) they were manufactured with the idea that they could be used at different locations; (3) the parties contemplated that the pumps would be removed for repairs or replacement; (4) the primary purpose of the sales agreements was the sale and purchase of the pumps assembled according to specifications and the installation of the pumps was merely incidental to that purpose; (5) the installation was for the convenience of the purchaser because of the great weight of the pumps; and (6) the sales agreements did not indicate that the pumps were intended to be treated as real property upon installation. 839 P.2d at 307.

The Supreme Court, in the Chicago Bridge case, found that Petitioner was a real property contractor, even when the materials were not installed in the state of Utah. In doing so, it relied on the fact that the tanks manufactured by Chicago Bridge, and which were installed by agents of Chicago Bridge in another state were "not readily removable" and they were not intended to be removed. 839 P.2d at 307.

The theory of taxing real property contractors was laid out in the BJ-Titan Services case where the court stated that contractors:

. . . purchased the materials not to resell them in their original form, but for the purpose of changing their nature from personal to real property. For this reason, the exemption for ingredients or component parts of tangible personal property does not apply to contractors. 842 P.2d at 827.

Clearly Petitioner herein is engaged in changing the nature from personal to real property. When the home is put on a crane and removed from the truck, that conversion process is almost

complete.

The Supreme Court has clearly set forth the law to be used in determining whether what Plaintiff does as an integral part of a real estate transaction and whether Petitioner is a real property contractor. The Utah State Tax Commission never made such an analysis, and never applied the law. The Tax Commission used its own method of analysis, which this Court characterized as an "'affixation' distinction". While this Court's ruling that such a distinction is not "unreasonable" might otherwise be correct, it cannot be construed to be either reasonable or correct when it simply does not conform to the Supreme Court's directives. Such a decision by the Utah State Tax Commission could only be upheld if they had analyzed the transaction under the guidelines given by the Utah Supreme Court and still rejected Petitioner's arguments. The fact that they have not been willing to do so makes their decision unreasonable, per se.

### POINT III

**GIVEN THE COURT'S RULING ON OTHER MATTERS, THE COURT'S FINDING THAT IT IS PETITIONER'S RESPONSIBILITY TO COLLECT AND PAY THE SALES TAX IS IN ERROR.**

Based upon the earlier parts of its ruling, which Petitioner does not here concede are correct, this court is correct in determining that it is the dealer who has "primary liability for the sales tax". slip op. p. 9. This Court is not correct,

however, in determining that Petitioner thus becomes a "retailer" for any purpose whatsoever. The parties have stipulated that a special rule exists in the case of contractors. That special rule allows the real property contractor to purchase building materials in a tax exempt transaction, and then to determine and pay the tax only upon the sale of that home to the ultimate buyer. That special rule is set out in the additional stipulated facts submitted with Petitioner's original brief, and also submitted herewith. Assuming (but not admitting) that the court is correct that Valgardson Housing Systems is merely selling building supplies to a contractor (the dealer) then the court is taxing the wrong transaction. The purchase of building supplies is tax exempt, and it is up to the dealer to determine and pay the tax.

#### CONCLUSION

Petitioners petition for a rehearing should be granted, the Court should re-examine the legal issues as set forth above, and the original decision herein should be vacated.

#### CERTIFICATION

Counsel for Petitioner hereby certifies, pursuant to Rule 35 of the Utah Rules of Appellate Procedure, this Petition for Rehearing is made in good faith, and is not made for the purposes of delay. Petitioner has previously paid all disputed taxes, and no collection action is pending.

DATED this 19<sup>th</sup> day of March, 1993.

MCCULLOUGH, JONES & IVINS

W. Andrew McCullough  
W. Andrew McCullough  
Attorney for Petitioner

CERTIFICATE OF SERVICE

I hereby certify that on the 19<sup>th</sup> day of March, 1993,  
I did mail two true and correct copies of the above and foregoing  
Reply Brief, postage prepaid to Clark Snelson, Attorney for  
Respondent, 36 South State Street, 11th Floor, Salt Lake City, Utah  
84111.

W. Andrew McCullough

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## ADDENDUM



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APPEALS SECTION  
STATE TAX COMMISSION

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BEFORE THE UTAH STATE TAX COMMISSION

STATE OF UTAH

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VALGARDSON HOUSING SYSTEMS,	:	ADDITIONAL STIPULATED
	:	FACTS
	:	
Petitioner,	:	
	:	
vs.	:	Appeal No. 91-1323
	:	
AUDITING DIVISION OF THE UTAH	:	
STATE TAX COMMISSION,	:	
	:	
Respondent.	:	

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COME NOW the parties to the above-entitled action and, in addition to the Stipulated Facts previously entered herein, agree and stipulate to the following facts:

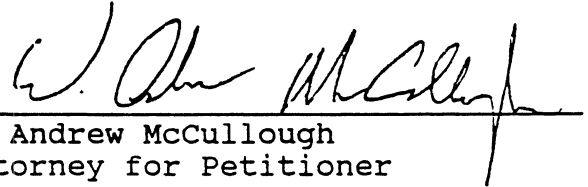
1. Petitioner purchases building materials in a tax exempt transaction.

2. Petitioner pays sales tax on the sales of his homes, based on total sales made during the period of each return, including cash, credit, installment and conditional sales made during that period. Sales tax is paid on 50% of the purchase price of the home, and including transportation costs (see previous Stipulated Facts Nos. 23, 24 and 25).

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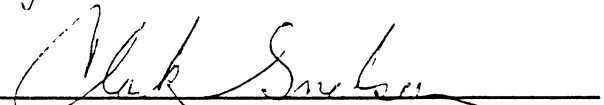
DATED this 14<sup>th</sup> day of May, 1992.

MCCULLOUGH, JONES & IVINS



W. Andrew McCullough  
Attorney for Petitioner

DATED this 18 day of May, 1992.



Clark L. Snelson  
Assistant Attorney General  
Attorney for Respondent

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