DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: June 9, 2005
Decision: MTHO #160
Tax Collector: City of Phoenix
Hearing Date: September 1, 2004

DISCUSSION

Introduction

On December 4, 2003, ***Taxpayer*** Resort ("Taxpayer") filed a protest of a denial by the City of Phoenix ("City") of a tax refund requested by the Taxpayer. After review, the City concluded on December 10, 2003 that the protest was timely and in the proper form. On December 15, 2003, the Municipal Tax Hearing Officer ("Hearing Officer") ordered the City to file a response to the protest on or before January 29, 2004. On January 21, 2004, the City requested an extension to file a response. On January 23, 2004, the Hearing Officer granted the City an extension until March 31, 2004. The City filed a response to the protest on February 27, 2004. On March 3, 2004, the Hearing Officer ordered the Taxpayer to file any reply on or before March 24, 2004. On March 8, 2004, a Notice of Tax Hearing ("Notice") scheduled the matter for hearing commencing on May 21, 2004. On May 17, 2004, the Taxpayer sent an email requesting the hearing be continued. On May 21, 2004, the Hearing Officer granted the Taxpayer's request to continue the hearing. On July 6, 2004, a Notice was issued setting the matter for hearing on August 30, 2004. On July 27, 2004, a Notice was issued rescheduling the hearing until September 1, 2004. Both parties appeared and presented evidence at the September 1, 2004 hearing. On September 3, 2004, the Hearing Officer indicated the parties had agreed to the following schedule: the Taxpayer would provide additional documentation requested by the City on or before October 1, 2004; the City would file a closing brief on or before November 1, 2004; and the Taxpayer would file a reply brief on or before December 16, 2004. On September 29, 2004, the Taxpayer provided its additional documentation. On October 29, 2004, the City sent an email requesting an extension of time for the closing brief. On November 2, 2004, the Hearing Officer revised the City's deadline for their closing brief to November 22, 2004 and the Taxpayer's reply deadline to January 6, 2005. On November 16, 2004, the City sent an email requesting another extension for the deadline of the closing brief. On November 18, 2004, the Hearing Officer revised the City's deadline for their closing brief to December 22, 2004, and the Taxpayer's reply brief to February 7, 2005. On December 15, 2004, the City sent an email requesting an additional extension for the closing brief. On December 15, 2004, the Hearing Officer revised the City's closing brief deadline to January 21, 2005 and the Taxpayer's reply brief deadline to March 9, 2005. On January 20, 2005, the City sent an email requesting another extension. On January 21, 2005, the Hearing Officer revised the City's closing brief deadline to January 28, 2005 and the Taxpayer's reply brief deadline to March 16, 2005. The City filed a closing brief on January 28, 2005. On March 10, 2005, the Taxpayer sent an email requesting an extension for the deadline for its reply brief. On March 14, 2005, the Hearing Officer revised the deadline for the Taxpayer's reply brief until April 15, 2005. On April 12, 2005, the Taxpayer filed its reply brief. On April 20, 2005, the Hearing Officer indicated the record was now closed and a written decision would be issued on or before June 6, 2005

City Position

City Code Section 14-560 (c)

In response to the Taxpayer's argument that City Code Section 14-560 (c) ("Section 560 (c)" has been rendered ineffective by Arizona Department of Revenue v. Canyoneers, Inc., 200 Ariz. 139, 23 p. 3d 684 (2201), the City argued the City's provisions are not similar and the reasoning of Canyoneers, supra, does not apply. The City indicated that Section 560 (c) does not permit a refund of taxes to a taxpayer unless the taxpayer can show that it will refund customers who have been charged the tax amounts refunded within 60 days. In this case, the City argued that the Taxpayer has provided no evidence that any taxes refunded will be returned to guests within sixty days of any refund by the City.

Records

The City asserted that City Code Section ("Section 350"), 14-360 ("Section 360"), and City Regulation 14-350.1 ("Regulation 350.1") provide specific guidance as the requirements for record keeping by taxpayers. Further, City Code Section 14-460 (b) ("Section 460 (b)") provides that the burden of proving that a sale of tangible personal property is not taxable retail sales is on the person who made the sale. The City argued that in this case with regard to the refunds recommended for denial, the Taxpayer has not provided documentation to meet its burden of proof.

Cancellation and Attrition Fees

These charges occur when groups contract with the Taxpayer for a block of rooms and fail to cancel by an agreed upon time in order to avoid the charge or when groups only use a portion of the rooms agreed upon, and held. City Code Section 14-200 ("Section 200") defines "gross income" to include all receipts. The City argued that the code definitions of "business," "hotel," and "occupancy" set forth in City Code Section 14-100 ("Section 100") supports the City's argument that the cancellation and attrition fees were taxable under the hotel activity pursuant to City Code Section 14-444 ("Section 444") and the transient hotel activity pursuant to City Code Section 14-447 ("Section 447"). The City extracted the following from copies of Letters of Agreements ("Agreements") between the Taxpayer and group customers. "Upon acceptance of this contract, we will remove from inventory and consider sold to you suite nights according to the following pattern:" The agreements go on to further state under the "Reduction of Suite Block and Food & Beverage Commitment" heading that "Should your utilization of suite nights fall below this commitment, a charge representing the contracted suite rate **plus tax**, per night will be posted to your master account for each suite night for which you have contracted hereunder but which you do not utilize." (Emphasis added) This is substantiated by the Taxpayer's documentation titled "Attrition/Performance Report" and the corresponding invoice copies. The Attrition/Performance Reports show the calculation of the room attrition and a separate charge for taxes which calculates to 12.07%, which represents the combined State/County/City rate for transient lodging. As a result, the City argued it is clear that the rooms were sold to the respective groups. As a result, the City asserted attrition and cancellation fees are taxable pursuant to Sections 100, 200, 445, and 447. The City recommended the refund be denied.

Food and Beverage Cancellation and Attrition Charges

The City noted that the Taxpayer had indicated at the hearing that food and beverage cancellation and attrition charges related to groups were also reported under the transient lodging classification. In response to the Taxpayer's argument that these charges are not taxable, the City argued the charges would be taxable under the restaurant/bar classification. The City argued that these charges are an integral part of operating the hotel's restaurant/bar business and the customer has paid for the right to acquire the food and beverages. The City reviewed customer agreements provided by the Taxpayer and determined the following: Under the heading "Reduction of Suite Block and Food & Beverage Commitment" the agreements state, "Planned banquet food & beverage revenues minimums are . . . All revenue figures are net and not inclusive of taxes, service charges. We agree to allow for a 10% reduction in these figures between now and . . . Should actual revenues fall below these figures, the difference will be posted t your master account." Based on the documentation provided, the City asserted that it could not be verified if tax was separately calculated, or self assessed. The City argued that if the tax was separately calculated and charged, then the tax reported under the transient lodging classification is due the City and the refund request should be denied pursuant to Section 560 (c). The City asserted that if the tax was self assessed, then a refund of the additional three percent for transient lodging should be refunded. The City indicated the Taxpayer would need to provide supporting documentation tying to tax worksheets so the City can verify the revenue was included in the transient lodging category.

Commission Revenue from ***Restaurant***

The Taxpayer informed the City that the Taxpayer had an agreement with ***Restaurant*** that allows hotel guests to charge meals at ***Restaurant*** to their hotel rooms. The Taxpayer would keep a portion of the meal charges as a commission. The City asserted that one of the major taxable activities of the Taxpayer is providing restaurant and bar service to guests and non-guests. The City argued that the Taxpayer's agreement with ***Restaurant*** permitted Taxpayer's customers to obtain meals from ***Restaurant*** in a similar manner as if they obtained the meals from Taxpayer's restaurants. The City asserted that Section 200 broadly defines the definition of gross income and as a result the City argued the commissions from ***Restaurant*** would be taxable under the restaurant/bar classification.

Transportation Services Revenue

According to the City, the Taxpayer indicated that tax was separately charged and collected on transportation services revenue. As a result, the City argued that the Taxpayer has not complied with Section 560 (c) and no refund can be granted.

Use Tax

The City reviewed documentation provided by the Taxpayer regarding use tax paid to six vendors. After review, the City concluded that the Taxpayer should be refunded $6,342.06 of use tax that was erroneously paid the City.

Company A Commissions

Based on documentation provided by the Taxpayer, the City was able to verify that the Taxpayer paid transient lodging tax on commissions received from ***Company A*** for in-room movies. The

City agreed that taxes on these revenues were improperly paid and recommended a refund of $2,404.13.

Taxpayer Position

The Taxpayer protested the denial by the City of a refund request in the amount of $167,967.53 for the period of July 1999 through December 2002. The refund request was for taxes paid for cancellation and attrition revenues, commission revenues from ***Company A***, commission revenues from ***Restaurant***, transportation services revenues, and use tax paid in error on purchases. The refund request for the respective revenues was $133,652.43, $3,905.97, $4,005.04, $21,721.68, and $4,682.41.

Cancellation and Attrition Fees

The cancellation fees are charged when a group reserves a block of rooms and then cancels the entire block of rooms after a specified date. According to the Taxpayer, the fee is usually based on the number of unsold room nights multiplied by the contracted group room rate. The Taxpayer indicated the cancellation fee may be adjusted if the Taxpayer is able to rent the previously reserved rooms to any new prospective guests. The Taxpayer indicated that Section 444 states the following: "The tax rate shall be at an amount equal to one and eight tenths percent of the gross income from the business activity upon every person engaging or continuing in the business of operating a hotel charging for longing and/or lodging space furnished to any person." Further, that Section 447 states the following: "In addition to the taxes levied as provided in Section 14-444, there is hereby levied and shall be collected an additional tax in an amount equal to three percent of the gross income from the business activity of any hotel engaging or continuing within the City the business of charging for lodging/or lodging space furnished to any transient. "Transient" means any person who, for the period of not more than 30 consecutive days, either at his own expense or at the expense of another, obtains lodging or the use of any lodging space in any hotel for which lodging or use of lodging space is made."

The Taxpayer argued that Section 447 does not apply to a group cancellations or attrition since the rooms were not received by a transient, guaranteed to a transient, nor used by a transient. Furthermore, the Taxpayer argued that Section 444 does not apply because no rooms were furnished to any person. The Taxpayer extracted the following from one of the Agreements: "The parties agree that should the Group cancel this commitment, actual damages would be difficult to determine. The following schedule represents a reasonable effort on behalf of the parties to establish its actual damages for such cancellations. It is agreed that such schedule shall represent liquidated damages to be paid by the Group for cancellation of this agreement."

The attrition fees are charged to a client when the actual number of rooms rented for a contracted event is less than the number originally specified by a contract. The fee is based on the number of unsold room nights multiplied by the contracted group room rate. The attrition fee may be adjusted if the Taxpayer is able to rent the rooms to any new prospective guests. In addition, the Agreement includes language on attrition fees. Under the Reservation Procedure section of the agreement it states that in order to guarantee a room, reservations are required to enable the hotel to assign individuals to the suite. "Any suite nights not reserved prior to September 19, 2002 or not prepaid . . . will be subject to the attrition provisions herein, and will be returned to our inventory for sale to others. In response to the City's arguments, the Taxpayer asserted the City's

privilege license tax is transactional tax and not a gross receipts tax. The Taxpayer argued that if the City's tax was meant to be a gross receipts tax then why doesn't the City impose the tax on all income received by hotels, etc. According to the Taxpayer, Arizona case law states that city taxes must be based on transactions and not on receipts.

Food and Beverage Cancellation and Attrition Charges

During the refund period, the Taxpayer paid taxes on food and beverage attrition and cancellation fees. The Taxpayer asserted that it did not prepare, furnish or serve the food or beverage to the group. According to the Taxpayer, the group failed to live up to its contractual obligation and as a result the Taxpayer imposed an amount for liquidated damages. The Taxpayer argued there was no taxable business activity and the taxes should be refunded. The Taxpayer indicated they had self-assessed and remitted the taxes to the City during the refund period.

Commission Revenue from ***Restaurant***

During the refund period, the Taxpayer received commissions from ***Restaurant*** for allowing hotel guests to charge meals at ***Restaurant*** on their hotel rooms. City Code Section 14-555 ("Section 555") assesses a tax on the gross income from the business activity of preparing or serving food or beverage in a restaurant. The Taxpayer asserts the food and beverage were not prepared and served by the Taxpayer. As a result, the Taxpayer argued the commissions were not taxable pursuant to Section 555.

Transportation Services Revenue

During the refund period, the Taxpayer separately charged and collected a tax on transportation services revenues. The Taxpayer argued that pursuant to the Canyoneers, supra it is entitled to the tax to be refunded.

Use Tax and ***Company A*** Commissions

The Taxpayer agreed with the amounts recommended by the City for tax erroneously paid on in-room movies and use tax during the refund period.

ANALYSIS

Cancellation and Attrition Fees

We concur with the City that these charges are properly taxable. Whether or not a customer uses room or not, they have paid for the right to have lodging space available. The nature of the hotel business is such that if the business loses a night of rental they can never recover those lost revenues. As a result, hotels like the Taxpayer utilize various charges such as cancellation and attrition charges to minimize the potential for lost revenue. While the Taxpayer argued these fees were penalties or liquidated damages it is clear from the evidence that the fees were normally calculated utilizing a per room charge. While there was evidence that the fees may be reduced, it is clear they would only be reduced if the Taxpayer had an opportunity to recover the revenues from other customers. Clearly these fees are an integral part of the business of operating a hotel and as such would be taxable pursuant to Sections 100, 200, 444, and 447. As a result, any refund is denied. We also conclude that even if these fees were not taxable the Taxpayer would

not be eligible for a refund because there was no evidence that the separate tax charged would be returned to customers pursuant to Section 560 (c).

Food and beverage Cancellation and Attrition Charges

We concur with the City that these charges are properly taxable. Similar to the cancellation and attrition charges for rooms, if the hotel loses a day of revenues and/or the facilities are not utilized to their full capacity, the Taxpayer would never be able to recover those lost revenues. As a result, we must conclude that the food and beverage cancellation and attrition charges are an integral part of the banquet/restaurant business of the Taxpayer and thus taxable pursuant to City Code Section 455. During the refund period, the Taxpayer actually paid the City a higher transient hotel tax and was eligible for a refund of excess taxes paid. However, the Taxpayer did not respond to the City's request for additional documentation to demonstrate that the tax was not separately charged. Further, the Taxpayer provided no evidence to demonstrate any tax would be refunded to customers. As a result, pursuant to Section 560 (c) any refund must be denied.

Commission Revenue from ***Restaurant***

We concur with the Taxpayer. If these revenues are taxable, the tax would fall on ***Restaurant*** and not the Taxpayer. These revenues are not related to any restaurant/bar activity of the Taxpayer. Any tax paid to the City during the refund period for these revenues should be refunded to the Taxpayer.

Transportation Service Revenues

We concur with the City. Based on the record, the Taxpayer separated charged City tax to its customers on these revenues. Since there was no evidence that the tax would be refunded to customers, we must deny any refund pursuant to Section 560 (c).

Use Tax and ***Company A*** Commissions

The parties were in agreement that a refund of erroneously paid use tax in the amount of $6,342.06 and erroneously paid tax on the commissions from ***Company A*** in the amount of $2,404.13 should be granted. We concur and approve the agreed upon refund amounts of $6,342.06 and $2,404.13.

FINDINGS OF FACT

1. On December 4, 2003, the Taxpayer filed a protest of a denial by the City of a tax refund requested by the Taxpayer.

2. After review, the City concluded on December 10, 2003 that the protest was timely and in proper form.

3. On December 15, 2003, the Hearing Officer ordered the City to file a response to the protest on or before January 29, 2004.

4. On January 21, 2004, the City requested an extension to file a response.

5. On January 23, 2004, the Hearing Officer granted an extension until March 31, 2004.

6. The City filed a response to the protest on February 27, 2004.

7. On March 3, 2004, the Hearing Officer ordered the Taxpayer to file any reply on or before March 24, 2004.

8. On March 8, 2004, a Notice was issued setting the matter for hearing on May 21, 2004.

9. On May 17, 2004, the Taxpayer sent an email requesting the hearing be continued.

10. On May 21, 2004, the Hearing Officer granted the request to continue the hearing before April 8, 2004, and a written decision would be issued on or before May 24, 2004.

11. On July 6, 2004, a Notice was issued setting the matter for hearing on August 30, 2004.

12. On July 27, 2004, a Notice was issued rescheduling the matter for hearing on September 1, 2004.

13. Both parties appeared and presented evidence at the September 1, 2004 hearing.

14. On September 3, 2004, the Hearing Officer indicated the parties had agreed to the following schedule: the Taxpayer would provide additional documentation requested by the City on or before October 1, 2004; the City would file a closing brief on or before November 1, 2004; and, the Taxpayer would file a reply brief on or before December 16, 2004.

15. On September 29, 2004, the Taxpayer provided its additional documentation.

16. On October 29, 2004, the City sent an email requesting an extension of time for the closing brief.

17. On November 2, 2004, the Hearing Officer revised the City's deadline for their closing brief to November 22, 2004 and the Taxpayer's reply deadline to January 6, 2005.

18. On November 16, 2004, the City sent an email requesting another extension for the dealing of the closing brief.

19. On November 18, 2004, the Hearing Officer revised the City's deadline for their closing brief to December 22, 2004, and the Taxpayer's reply brief to February 7, 2004.

20. On December 15, 2004, the City sent an email requesting an additional extension for the closing brief.

21. On December 15, 2004, the Hearing Officer revised the City's closing brief deadline to January 21, 2005 and the Taxpayer's reply brief deadline to March 9, 2005.

22. On January 20, 2005, the City sent an email requesting another extension.

23. On January 21, 2005, the Hearing Officer revised the City's closing brief deadline to January 28, 2005 and the Taxpayer's reply brief deadline to March 16, 2005.

24. The City filed a closing brief on January 28, 2005.

25. On March 10, 2005, the Taxpayer sent an email requesting an extension for the deadline for its reply brief.

26. On March 14, 2005, the Hearing Officer revised the Taxpayer's reply brief deadline until April 15, 2005.

27. On April 12, 2005, the Taxpayer filed its reply brief.

28. On April 20, 2005, the Hearing Officer indicated the record was now closed and a written decision would be issued on or before June 6, 2005.

29. Cancellation fees are charged when a group reserves a block of rooms and then cancels the entire block of rooms after a specific date.

30. Cancellation fees are usually based on the number of unsold room nights multiplied by the contracted group room rate.

31. Attrition fees are charged to a client when the actual number of rooms rented for a contracted event is less than the number originally specified by a contract.

32. Attrition fees are based on the number of unsold room nights multiplied by the contracted group room rate.

33. A separate tax was charged on the cancellation and attrition fees.

34. There was no evidence to show the taxes on food and beverage cancellation and attrition charges were self assessed and not separately charged.

35. Pursuant to an agreement with ***Restaurant***, the Taxpayer would keep a portion of the restaurant charge as a commission.

36. The Taxpayer separately charged and collected tax on transportation services revenues.

37. During the refund period, the Taxpayer erroneously paid to the City a use tax of $6,342.06 and a transient lodging tax of $2,404.13 on commissions received from ***Company A***.

38. There was not evidence presented by the Taxpayer to demonstrate that any separately charged tax would be refunded to customers.

CONCLUSIONS OF LAW

1. Pursuant to ARS Section 42-6056, the Municipal Tax Hearing Officer is to hear all reviews of petitions for hearing or redetermination under the Model City Tax Code.

2. Cancellation and attrition fees are an integral part of the business of operating a hotel and as such would be taxable pursuant to Section 100, 200, 444, and 447.

3. The Taxpayer's request for a refund of taxes paid on cancellation and attrition fees should be denied.

4. Pursuant to Section 560 (c), no refunds are to be paid when the Taxpayer has collected, by separately stated itemization, the amount of such ax, unless the Taxpayer can present documentation satisfactory to the City that the taxes will be refunded to customers within sixty days of receipt of the refund.

5. The Taxpayer has presented no documentation to demonstrate any itemized taxes would be refunded to customers.

6. The burden is on the Taxpayer pursuant to Sections 350, 360, 460 (b), and Regulation 350.1 to maintain and provide suitable books and records to support any refund request.

7. The Taxpayer has failed to meet its burden of proof of demonstrating that the taxes on food and beverage cancellation and attrition charges were not separately charged to customers.

8. The Taxpayer's protest should be denied, in part, and granted, in part, consistent with the Discussion, Findings, and Conclusions, herein.

ORDER

It is therefore ordered that the December 4, 2003 protest by ***Taxpayer*** Resort of a denial of a refund claim by the City of Phoenix is hereby denied, in part, and granted, in part, consistent with the Discussion, findings, and conclusions, herein.

It is further ordered that the City of Phoenix shall provide a refund to ***Taxpayer*** Resort consistent with the Discussion, findings, and conclusions, herein.

It is further ordered that this Decision is effective immediately.

Jerry Rudibaugh
Municipal Tax Hearing Officer