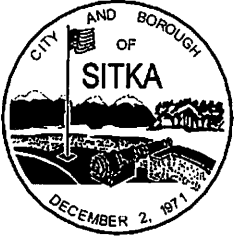


POSSIBLE MOTION

I MOVE TO adopt the Chief Finance and Administrative Officer's interpretation of the term "sales unit" as set forth in Sitka General Code 4.09.100 (N), and, further clarify the term "sale unit" as it pertains to the provision of services and bundled invoices.



City and Borough of Sitka

100 Lincoln Street • Sitka, Alaska 99835

MEMORANDUM

To: Mayor Hunter and Assembly Members
Keith Brady, Municipal Administrator

From: Jay Sweeney, Chief Finance and Administrative Officer

Date: September 20, 2017

Subject: Adopt Sales Tax Interpretation 17-02

1. Issue:

The Finance Director has made a sales tax regulatory interpretation which must, per the Sitka General Code (SGC), be brought to the Assembly for adoption or rejection. The interpretation pertains to what, exactly, constitutes a "sale unit", as set forth in SGC 4.09.100 (N), and, to further clarify the term "sale unit" as it pertains to the provision of services and bundled invoices.

2. Facts:

- A. SGC 4.09.400, Rules and Regulations, provides authority to the Finance Director to interpret the meaning and applicability of sales tax regulations to specific situations requiring an interpretation and decision. The interpretation and decision rendered are subsequently required to be submitted to the Assembly for adoption or rejection.

The SGC citation is as follows:

4.09.400 Rules and regulations

The finance director shall from time to time cause to be promulgated rules and regulations as are necessary and advisable to provide for the application and interpretation of this chapter and to submit them to the assembly for its adoption or rejection, and to cause to be provided methods and forms for reporting and collecting the tax in accordance with this chapter and regulations. (Ord. 03-1758 § 4(B), 2004.)

- B. In response to questions raised as to the meaning of the term "sales unit" as set forth in sales tax exemption N, Over (SGC 4.09.100 N), Over Three Thousand Dollars on Sales and Rents of Tangible Personal Property and on Sales of Services, and Over Three Thousand Dollars in Rent or Lease of Real Property on a Monthly Basis (*note: will change to \$12,000 on October 1, 2017*), described in the attached Interpretation, I have interpreted the meaning and intent of the Sitka General Code to be the following:

- a. Extra services that are provided in addition to those initially agreed upon at the time of the provision of the original services, or, that are invoiced on a cost plus materials basis, constitute a separate sales unit and are to be taxed as a separate sale. *An example would be an agreement for roof shingle replacement entered into after gutter cleaning services were performed, but are all invoiced on the same sales invoice.*
- b. Each instance in which tangible property, which is sold and invoiced on one sales slip, but which is delivered or for which ownership changes hands over the course of more than one day, constitutes a separate sales unit and shall be taxed as a separate sale. *An example is the sale of a large quantity of rock, invoiced on one single invoice, but which is delivered over the course of weeks/months.*
- c. Each single rental of commercial property for a period not to exceed 30 days shall constitute a separate sales unit, even if governed by a long-term lease or rental contract and invoiced on a single invoice. *An example is an annual lease of commercial property invoiced on one single invoice.*

3. Discussion:

- A. In conjunction with the increase of the taxable sales transaction limit to \$12,000 (effective October 1, 2017), the Finance Department has received several inquiries as to what comprises a "sales unit" for purposes of determining what portions of a sales transaction are taxable and exempt. In providing answers to these questions, the Finance Director has had to interpret the meaning of the term "sales unit" as set forth in SGC 4.09.100 (N).
- B. In order to reduce the total amount of a transaction including tax to customers and thereby create a value proposition and competitive edge, some sellers will occasionally try to find interpretative loopholes in the SGC which allow for some element of the total sales price to become tax exempt. When instances of these interpretative loopholes arise, they require additional interpretation as to the intent of the code. The definition of the term "sales unit" is one such loophole.
- C. The interpretive issues surrounding the term "sales unit" have taken different turns, but they all share one element in common: seeking to bundle multiple sales, performances of services, and rentals of real property into one single invoice for the purposes of having some portion of the total sale exempt from taxation (due to the "sales unit" being in excess of the taxable transaction limit).
- D. Historically, when questions as to of the application of sales tax code to individual seller circumstances arise, two common themes are found:
 - a. The seller needs an immediate answer and can't wait until the matter is presented to the Assembly at its next meeting, which could be as much as three weeks in the future. For this reason, the Finance Director was afforded

the ability to make interpretations as set forth in SGC 4.09.400.

- b. Extremely fine parsing of ***Exactly*** what is meant by a term or phrase is discussed. Even when code is carefully crafted, circumstances consistently arise wherein some unanticipated meaning or understanding surfaces. Such is the case with SGC 4.09.100 (N) 1, wherein the code states “...***although this exemption does not apply if any portion of the invoice or sales slip refers to more than one business day...***” This section of the code seemingly deals with the issue of bundling over time; however, a question has been raised as to whether the intent is to limit transactions in which no time limit is specified on the invoice or sales slip, yet delivery is made over a lengthy period of time. An example would be the sale of rock in which the sales slip says simply 1,000 yards of crushed D-1, but, which is negotiated to be delivered over the period of months and such negotiation is not specifically indicated on the sales slip. This transaction could, under some interpretation and parsing, be read to mean that, since the sales slip did not specifically refer to more than one business day, the entire sale is one sales unit and, therefore, subject to the taxable transaction limit. Hence, precise additional interpretation is required

- E. If the Assembly does not adopt the recommended interpretation or set forth an alternative interpretation, the precise meaning of the term “sales unit”, in certain contexts, will remain vague and undefined. This will result in additional staff time in the future spent revisiting this same issue, and, potential non-collection of sales taxes.

4. Analysis of Alternatives (Pros/Cons):

- A. Adoption of the Finance Director’s interpretation will clarify the meaning of a portion of the sales tax code interpretation which has been vague and, therefore, has led to questions, confusion, and possible loss of legitimate sales tax revenues. No additional staff time or expenditure will be required to adopt the recommended alternative.
- B. Rejection of the Finance Director’s interpretation will lead to continued vagueness and uncertainty as to the meaning of the term “sales unit”, unless the Assembly adopts a different interpretation.
- C. Adoption of a different interpretation of the term “sales unit” on the fly, without adequate research and contemplation, could lead to additional vagaries as to intent and meaning, causing the issue to potentially return to the Assembly again.

5. **Recommendation:** Administration recommends that the Assembly adopt the Finance Director’s Sales Tax Interpretation 17-02.