FEBRUARY 2024

THE BR STATE + LOCAL TAX SPOTLIGHT

BLANKROME

CONTENTS

STATE + LOCAL TAX TEAM:

Craig B. Fields | craig.fields@blankrome.com
Nicole L. Johnson | nicole.johnson@blankrome.com
Mitchell A. Newmark | mitchell.newmark@blankrome.com
Irwin M. Slomka | irwin.slomka@blankrome.com
Eugene J. Gibilaro | eugene.gibilaro@blankrome.com
Kara M. Kraman | kara.kraman@blankrome.com
Joshua A. Sivin | joshua.sivin@blankrome.com
Philip M. Tatarowicz | phil.tatarowicz@blankrome.com
Melanie L. Lee | melanie.lee@blankrome.com

Note from the Editors

By Joshua M. Sivin and Melanie L. Lee

Welcome to the February 2024 edition of *The BR State + Local Tax Spotlight.* We know the importance of remaining up-to-date on State + Local Tax developments, which appear often and across numerous jurisdictions. Staying informed on significant legislative developments and judicial decisions helps tax departments function more efficiently, along with improving strategy as well as planning. That is where *The BR State + Local Tax Spotlight* can help. In each edition, we will highlight important State + Local Tax developments that could impact your business. In this issue, we will be covering:

- Pennsylvania Commonwealth Court Affirms That Pittsburgh's Tax on Only Nonresident Athletes Violates State's Uniformity Clause
- California Appeals Court Declines Locality's Request to Rewrite Unlawful Tax Law
- Arizona Appellate Court Finds Online Travel Companies Not Subject to Tax on Hotel Operators

We invite you to share *The BR State + Local Tax Spotlight* with your colleagues and visit Blank Rome's State + Local Tax webpage for more information about our team. Click here to add State + Local Tax to your subscription preferences.

Co-Editors, *The BR State + Local Tax Spotlight*

JOSHUA M. SIVIN
Of Counsel
212.885.5025
joshua.sivin@blankrome.com

MELANIE L. LEE
Associate
212.885.5371
melanie.lee@blankrome.com

CRAIG B. FIELDS
PARTNER

Pennsylvania Commonwealth Court Affirms That Pittsburgh's Tax on Only Nonresident Athletes Violates State's Uniformity Clause

By Craig B. Fields

Although only some states have a uniformity clause in their constitutions, for those that do, it can be a powerful tool in challenging a tax. This was recently demonstrated in *National Hockey League Players' Ass'n v. City of Pittsburgh,* No. 1150 C.D. 2022 (Commonwealth Ct., Jan. 10, 2024), where the Commonwealth Court affirmed a trial court and held that Pittsburgh's Non-Resident Sports Facility Usage Fee ("Facility Fee") violates Pennsylvania's Uniformity Clause.

Facts: Pittsburgh enacted the Facility Fee whereby nonresidents of Pittsburgh who use the City's sports venues to engage in an athletic event or performance for remuneration are subject to a three percent assessment on personal income earned while in Pittsburgh. Similarly situated resident athletes of Pittsburgh are not subject to the Facility Fee. Instead, resident athletes are subject to a one percent earned income tax.

The National Hockey League Players' Association, Major League Baseball Players' Association, National Football League Players' Association, and a nonresident athlete from each association challenged the Facility Fee arguing that it was, in reality, a tax and that it violated the Uniformity Clause of the Pennsylvania Constitution.

Decision: Although Pittsburgh had argued below that the Facility Fee was a fee and not a tax, it now conceded that it was indeed a tax. The Court found that as a tax, the Facility Fee violated the Uniformity Clause, which requires that taxes be uniform upon the same class of subjects, although there is an exception where there is a non-arbitrary, reasonable, and just basis for the disparate treatment.

> **The Court held that the Facility Fee was facially discriminatory since it levies a three percent income tax on nonresidents in comparison to the City's one percent income tax on residents.**

The City's attempt to justify the different tax rates by asserting that resident athletes also pay a two percent income tax to the Pittsburgh school district was rejected since that two percent tax is levied by the school district, not Pittsburgh, and is used to directly fund the schools. Moreover, the school district is statutorily prohibited from imposing the tax on nonresidents. According to the Court, "[r]ough uniformity is not achieved where only one class of taxpayers—nonresidents—is assessed a 2% tax on income derived from its use of the Facilities."

The City's attempt to have portions of the Facility Fee severed by having the Court remove the word "non-resident" from the statute was also rejected. First, the legislation authorizing the Facility Fee only provided for its assessment on nonresidents. Moreover, the legislation explicitly provided that if the Facility Fee was invalidated by a court, then the exemption for nonresidents from the one percent earned income tax no longer applied. This, the Court found, clearly demonstrated that the General Assembly preferred that the Facility Fee be stricken entirely if held unconstitutional.

One judge dissented, asserting that the Facility Fee did not violate the Uniformity Clause since both resident and nonresident athletes ultimately paid a three percent tax on their income.

EUGENE J. GIBILARO
PARTNER

California Appeals Court Declines Locality's Request to Rewrite Unlawful Tax Law

By Eugene J. Gibilaro

How far should courts go to save tax laws that are plainly unlawful? In a case recently decided by an intermediate appeals court in California, a California locality, the City of Moreno Valley, asked the court to rewrite a local ordinance "to convert the tax [to be imposed] from an unlawful sales and use tax to a lawful transactions and use tax." *City of Moreno Valley v. California Dep't of Tax and Fee Admin.,* C097747, Super. Ct. No. 34-2022-80003915-CU-WM-GDS (Jan. 16, 2024). The Court declined the City's request, finding that the proper role of the courts "is fundamentally to interpret laws, not to write them," and that it was inappropriate in this case for the Court to exercise "the extraordinary power" to rewrite the City's ordinance. This case is a reminder that words have meaning and if a taxing authority is disregarding the plain meaning of the law, taxpayers should be prepared to fight back.

California law permits localities to impose two similar types of taxes on retail transactions: (1) a sales and use tax ("SUT"); and (2) a transactions and use tax ("TUT"). For localities that impose both an SUT and a TUT, a consumer's receipt from a retail purchase in the locality will include charges for both SUT and TUT (in addition to charges for the state-level sales and use tax). California law states that a locality's SUT rate may not exceed 1.25 percent and its TUT rate may not exceed two percent. Moreover, no locality may "impose, extend, or increase any general tax unless and until the tax is submitted to the electorate and approved by a majority vote."

In 2021, the City declared an ongoing fiscal emergency and called a special election for the City's voters to consider a measure to increase the City's SUT rate from one percent to two percent. The City's voters approved the measure and proposed ordinance. However, the California Department of Tax and Fee Administration, which administers and collects local SUT and TUT on behalf of localities, informed the City that it was unable to administer the tax as written because it imposed a SUT rate of two percent, which exceeded the maximum 1.25 percent rate permitted by State law.

The City Council responded by adopting a revised ordinance to impose a TUT at a rate of one percent (the City did not previously impose a TUT). The City argued that its imposition of a TUT at a rate of one percent in lieu of increasing the SUT from one percent to two percent did not require new voter approval because "the voters had effectively already approved the new ordinance because it was 'consistent with the intent'" of the approved measure to increase taxes on retail transactions by one percent. The City asked the Court to declare that the approved measure validly imposed a one percent TUT and to rewrite the City's ordinance as needed to make the ordinance lawful.

> **The Court rejected the City's invitation to rewrite the ordinance to save it from being invalid under California law.**

The Court found that while "[t]he City's voters were no doubt misguided in believing they could enact a two percent tax under the [SUT] law," that consideration was insufficient in itself "to trigger the absurdity doctrine and allow a wholesale rewriting of the ordinance." The Court also concluded that judicial reformation of the ordinance was not proper because the Court was "unable to conclude with confidence that the City's voters would support [the Court's] rewriting the ordinance to impose a tax that the voters never considered and that is materially different from the tax they approved."

JOSHUA M. SIVIN
OF COUNSEL

Arizona Appellate Court Finds Online Travel Companies Not Subject to Tax on Hotel Operators

By Joshua M. Sivin

Last month, an Arizona appellate court found that online travel companies such as Orbitz and Expedia ("OTCs") are not entities that operate hotels nor cause hotels to be operated and therefore are not subject to Tucson's tax applicable to such entities. *City of Tucson v. Orbitz Worldwide, Inc., et. al.* (Ariz. Ct. Appeals, Division One, Jan. 11, 2024).

Facts: OTCs operate websites where travelers may book hotel rooms. In earlier litigation ("Prior Litigation"), several Arizona cities sought to impose tax on OTCs under sections 444 and 447 of Arizona's Model City Tax Code ("MCTC"). Section 444 imposes a tax on "the gross income from the business activity upon every person engaging…in the business of operating a hotel." Section 447 taxes "the gross income from the business activity of any hotel." The MCTC defines "person" to include "broker[s]."

In the Prior Litigation, the Arizona Supreme Court held that OTCs were liable for tax under Section 444 as brokers but were not liable for tax under Section 447, reasoning that Section 444 imposes "tax liability on *any* 'person'—not just a hotel owner or operator—that engages for profit in business activities that are central to keeping brick-and-mortar lodging places functional or in operation." The Court held that Section 447 did not apply to brokers (such as OTCs) because it only taxed "the gross income from the business activity of any hotel."

The statute at issue in the current litigation, Section 19-66, applies to "every person who operates" a hotel or "causes [a hotel] to be operated." Tucson argued that because Section 19-66 and Section 444 both used the language "every person," Section 19-66 should apply to OTCs. The superior court agreed and ruled in favor of Tucson.

Decision: The Appellate Court reversed, finding that Section 19-66 does not mirror Section 444, despite the fact that both statutes utilize the same "every person" language. The Court found "[a]s written, § 19-66 refers to only two taxpayer categories: 'every person' who operates hotels, and 'every person' who "cause[s] [hotels] to be operated.' The absence of 'business activity' and 'business of' from § 19-66(a) eliminates all others as subjects of the tax. Thus, § 19-66 will apply only if OTCs like Expedia are hotel operators or if they cause hotels to be operated."

> **The Court went on to determine that OTCs are not hotel operators because OTCs are not proprietors of a hotel nor a non-employee managing agent who performs the proprietor's functions. OTCs are brokers. The Court further determined that OTCs do not cause hotels to be operated because the language in Section 19-66 "shows the tax is directed at hotel operations, not adjacent business activities."**

In analyzing the language of Section 19-66 and comparing it to Sections 444 and 447, the Court found:

> The text therefore deviates from the restrictive formulation of [Section] 447, which only imposes a tax on *"any hotel."* But it also departs from the broader language of [Section] 444 which taxes "the gross income from *the business activity* [of] every person engaging in or continuing in *the business of* operating a hotel." The omission of any reference to "business activity" and "business of" operating hotels is significant.

Takeaway: Words in a statute matter, and statutes must be analyzed individually, even where similar language is used. In this case, because Section 19-66 applied only to "every person who operates" a hotel or "causes [a hotel] to be operated," and not to the "business activity upon every person engaging…in the business of operating a hotel," like the tax in Section 444, OTCs which neither operate hotels nor cause hotels to be operated were not subject to tax.

What's Shaking: Blank Rome's State + Local Tax Roundup

Blank Rome's nationally prominent State + Local Tax attorneys are thought leaders in the community as frequent guest speakers at various local and national conferences throughout the year. Our State + Local Tax attorneys believe it is necessary to educate and inform their clients and contacts about topics that will impact their businesses. We invite you to attend, listen, and learn as our State + Local Tax attorneys interpret and discuss key legal issues companies are facing and how you can put together a plan of action to mitigate risk and advance your business in accordance with state and local tax laws.

Charter Ineligible for Tech Co. Tax Break, NY Tribunal Says

- Blank Rome State + Local Tax partner Mitchell A. Newmark was interviewed by *Law360 Tax Authority* discussing a recent decision by the New York State Tax Appeals Tribunal. To learn more, please click here.

Local Tax Update

- Blank Rome State + Local Tax partner Nicole L. Johnson will serve as a speaker at the Tax Executives Institute ("TEI") 74th Midyear Conference, being held March 17 through March 20, 2024, in Washington, D.C. To learn more, please click here.

BLANKROME