

AGENDA ITEM SUMMARY

August 18, 2015

City Council

STAFF

Peggy Streeeter, Senior Sales Tax Auditor
Mike Beckstead, Chief Financial Officer

SUBJECT

First Reading of Ordinance No. 097, 2015, Amending Provisions in Articles III and IV of City Code Chapter 25 Concerning the Exemption of Charitable Organizations from the City's Sales and Use Tax and Lodging Tax.

EXECUTIVE SUMMARY

The purpose of this item is amend the definition of "charitable organization" as used in the City Code's sales and use tax and lodging tax provisions in order to mitigate the impact of current Colorado case law on a substantial number of the City's current tax exempt charitable organizations. Colorado case law was recently discovered to have a substantial impact on staff's interpretation of the charitable organization definition. Code changes related to the City's sales and use taxes were discussed with the Council Finance Committee on June 23, 2015, and the Committee concurred with the recommendation and supported staff bringing an ordinance to Council.

STAFF RECOMMENDATION

Staff recommends adoption of the Ordinance on First Reading.

BACKGROUND / DISCUSSION

Chapter 25 of the City Code allows organizations that meet the definition of a "charitable organization" to purchase tangible personal property for use in the organizations' activities free from the City's sales and use taxes and lodging tax.

CURRENT CITY CODE LANGUAGE

General Information

City Code Section 25-71 defines a "charitable organization" as:

"Charitable organization shall mean any entity which: (i) has been certified as a not-for-profit organization under Section 501(c)(3) of the Internal Revenue Code; and (ii) is a religious or charitable organization. As used in this definition, a "charitable organization" is an organization which exclusively, and in a manner consistent with existing laws and for the benefit of an indefinite number of persons, freely and voluntarily ministers to the physical, mental or spiritual needs of persons, and which thereby lessens the burdens of government."

The City currently has 295 charitable organizations that hold an "exempt organization license" issued by the City. In general terms, the Code allows these organizations to make purchases free of sales and use tax but does not exempt them from collecting sales tax on transactions. For example, if a charitable organization, as defined by City Code, purchases materials for use in its activities, it does not pay sales tax. However, if the

organization sells tangible goods, for example in a book sale, it is generally still required to collect and remit the tax to the City. This is an important distinction.

The process to become an exempt organization with the City is as follows:

- Application submitted with following documents:
 - List of officers
 - Articles of Incorporation
 - 501(c)3 letter
 - Bylaws
 - Colorado Certificate of Incorporation
 - Copy of State exemption certificate
 - Financial statements
- Application reviewed by staff for completeness and determines if organization meets definition of “charitable organization”
- Application approved or denied (3 year renewable period). If denied, organization can request a hearing with the Financial Officer or designee

The City’s lodging tax provisions, in Article IV of City Code Chapter 25, do not define “charitable organization.” Instead, Code Section 25-243(2) generally exempts “religious, charitable and eleemosynary corporations,” without definition, from payment of the lodging tax.

PROPOSED CODE AMENDMENT:

This Ordinance will amend City Code to exempt any entity from the City’s sales and use taxes and lodging tax, whether religious or secular, that has been granted a sales tax exemption by the State of Colorado based on C.R.S. Section 39-26-718(1)(a), which reads:

“(1) The following shall be exempt from taxation under the provisions of part 1 of this article:

(a) All sales made to charitable organizations, in the conduct of their regular charitable functions and activities; except that any veterans' organization that qualifies as a charitable organization pursuant to section 39-26-102 (2.5) shall be exempt from taxation under the provisions of part 1 of this article only for the purpose of sponsoring a special event, meeting, or other function in the state of Colorado that is not part of the organization's regular activities in the state;”

The State of Colorado defines “charitable organization” in C.R.S. Section 39-26-102(2.5) as:

"Charitable organization" means any entity organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office, or any veterans' organization registered under section 501 (c) (19) of the "Internal Revenue Code of 1986", as amended, for the purpose of sponsoring a special event, meeting, or other function in the state of Colorado so long as such event, meeting, or function is not part of such organization's regular activities in the state.”

CITY FINANCIAL IMPACTS

There will be minimal revenue loss; however, the amount is difficult to quantify. In many cases the City is not capturing the revenue because vendors accept the State’s exemption certificate for City sales and lodging

taxes when purchases are made regardless of whether the organization has an exempt organization license from the City. Based on organizations who have been denied exemption based on the current interpretation of the definition, we would estimate revenue loss to be approximately \$30K per year.

BOARD / COMMISSION RECOMMENDATION

The proposal to amend the definition was presented to the Council Finance Committee (CFC) on June 23, 2015. Three options were presented and CFC supported the option presented in this Ordinance as related to sales and use taxes. The lodging tax was not discussed with the CFC, but staff is recommending that the same definition for “charitable organization” be used for lodging tax to be consistent with the City’s sales and use taxes.

ATTACHMENTS

1. Council Finance Committee minutes, June 23, 2015 (PDF)



ATTACHMENT 1

Finance Administration

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Fort Collins, CO 80522

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fcgov.com

Council Audit & Finance Committee

Minutes

06/23/15

2:30 – 4:30 p.m.

Community Room

Council Attendees: Mayor Wade Troxell, Gerry Horack, Ross Cunniff

Staff: Mike Beckstead, Jeff Mihelich, John Duvall, John Voss, Josh Birks, Jessica Ping-Small, Travis Storin, Peggy Streeter, Nancy James

Others: Kevin Jones – Chamber of Commerce

APPROVAL OF MINUTES

Ross Cunniff made a motion to approve the May 18, 2015 Council Finance Committee minutes. Gerry Horack made a second to the motion. The minutes were approved unanimously.

Mike indicated that he will be deferring the July 20th calendar item – Long Term Revenue Diversification due to Jessica leaving her position on July 3rd; she has accepted a job with Advanced Energy. The posting for her position will be going out later this week or early the week of June 29th.

EXEMPT ORGANIZATION – POTENTIAL CODE UPDATES

Chapter 25 of the Municipal Code allows organizations that meet the definition of *charitable*, per city code, to purchase tangible personal property for use in the organizations' activities free from city of Fort Collins sales and use tax. Recently, Colorado case law was discovered that may have a substantial impact on staff's interpretation of the charitable organization definition. Staff is recommending City Council consider amending the code to mitigate the impact of the case law to a substantial number of the city's 300 exempt organizations.

The general direction sought and specific questions were proposed to CFC:

- Does CFC support potential code changes to amend the definition of *charitable organization*?
- Does the CFC support one of the options presented by staff?

The current Code allows the entities exemption from paying sales and use tax on purchases but does not exempt them from collecting sales tax if selling tangible goods.

Issue to Address:

- In fall of 2014 staff denied an application for exemption based on definition.
- During appeal process, City Attorney’s Office discovered a ruling from the CO Supreme Court:
 - Definition of charitable organization the same as Fort Collins
 - CO Supreme Court interpreted definition differently than staff has historically

Impact of Ruling: 23% (70) of City Exempt Organizations would no longer qualify under existing definition.

Staff feels that this would have a big impact locally, thus is requesting that a review be made to the current code and consider the following options:

Option 1) No code change

Option 2) Redefine “charitable organization” to align with the past application of the definition

Option 3) Amend code to exempt any religious or charitable organization that has been granted tax exempt status by the state or eligible for tax exemption under state law.

Secular charities and religious organizations have to be treated equally by definition. Moving forward, there are pros and cons in regard to each option.

Staff’s recommendation is to take the 3rd option, which would amend code to exempt any entity granted tax exemption from the State:

- Allows existing organizations to retain exemption
- Supports local charitable organizations
- Reduce staff time and subjectivity of definition
- Simplified process for charitable organizations
- Diminishes confusion for retailers

After discussion, it was determined that CFC would take staff’s recommendation to take Option #3. John Duvall stated that by amending the code to include the state’s definition, any entity that meets the City’s definition of the code will also meet the state’s definition. When the state amends their code, the City will then have to amend its code as well.

2014 YEAR END FINANCIAL HIGHLIGHTS

A recap of revenue, expenditures and debt was reviewed by CFC. The financial condition of the City continues to be healthy, as reported by John Voss. Revenues increased as did expenditures. The population continues to grow, and with it, a demand for more services. Outstanding debt continues to decline.

There are two broad categories in accounting – Governmental Activities and Enterprise Activities. Governmental activities are described as those activities that do not lend themselves to be fully funded by User Fees and are wholly or partially tax supported (Transportation, Police, Fire, Parks, Natural Areas, etc.) Enterprise activities are

ORDINANCE NO. 097, 2015
OF THE COUNCIL OF THE CITY OF FORT COLLINS
AMENDING PROVISIONS IN ARTICLES III AND IV OF
CITY CODE CHAPTER 25 CONCERNING THE EXEMPTION OF CHARITABLE
ORGANIZATIONS FROM THE CITY'S SALES AND USE TAXES AND LODGING TAX

WHEREAS, under City Code Sections 25-73(c)(6), 25-74(b)(9) and 25-94(a), a "charitable organization," as this term is defined in Code Section 25-71, that obtains a "exempt organization license" from the City is exempt from the City's sales and uses taxes for the organization's purchases and its use in the City of tangible personal property and taxable services; and

WHEREAS, Code Section 25-71 currently defines a "charitable organization" as any religious or secular entity that meets all of the following requirements: (i) it is a non-profit organization; (ii) it is recognized under the Internal Revenue Code as a Section 501(c)(3) organization; and (iii) it is an organization that "exclusively, and in a manner consistent with existing laws and for the benefit of an indefinite number of persons, freely and voluntarily ministers to the physical, mental or spiritual needs of persons, and which thereby lessens the burdens of government;" and

WHEREAS, the City's past interpretation and application of this definition has resulted in 295 organizations currently having a valid exempt organization license issued by the City, which license must be renewed by the organization every three years; and

WHEREAS, in a 2009 decision the Colorado Supreme Court considered this same definition of "charitable organization" used by the City of Pueblo in its sales and use tax code and interpreted and applied it much more narrowly than Fort Collins has previously done; and

WHEREAS, under the Supreme Court's interpretation and application of the City's current definition, a significant number of the 295 organizations that have a exempt organization license from the City would no longer qualify for this license and, consequently, would no longer be exempt from payment of the City's sales and use taxes; and

WHEREAS, in light of the Supreme Court's interpretation, City staff is recommending that the City's definition of "charitable organization" be amended to insure that the organizations in the City that currently have an exempt organization license continue to qualify for it and that the new definition allow for the ease of the City's administration in its issuance of exempt organization licenses; and

WHEREAS, to accomplish this, City staff is recommending that the City's definition be amended to be consistent with the State of Colorado's definition for "charitable organization" as used in its sales and use tax statutes, and to do this by defining "charitable organizations" as any entity that has and maintains a current sales tax exemption certificate from the Colorado Department of Revenue; and

WHEREAS, at its June 13, 2015, meeting, the Council Finance Committee considered these recommendations, as well as other options presented to it by City staff, and the Committee directed staff to bring forward to City Council an ordinance that would amend the City's definition as recommended by staff; and

WHEREAS, staff is also now recommending that this new definition for "charitable organization" be included and used for those "religious, charitable and eleemosynary corporations" now exempt from the City's lodging tax in City Code Section 25-243(2), so that the charitable organizations exempt from the City's lodging tax are consistent with those exempt from the City's sales and use taxes; and

WHEREAS, the Council finds that it is in the best interest of the City and its citizens that the City amend its definition of "charitable organization" for sales and use tax and lodging tax purposes to be consistent with the definition used for this term by the State of Colorado in its sales and use tax statutes.

NOW, THEREFORE, BE IT ORDAINED BY THE COUNCIL OF THE CITY OF FORT COLLINS as follows:

Section 1. That the definition of "charitable organization" contained in Section 25-71 of the Code of the City of Fort Collins is hereby amended to read as follows:

Charitable organization shall mean any entity ~~which: (i) has been certified as a not-for-profit organization under Section 501(c)(3) of the Internal Revenue Code; and (ii) is a religious or charitable organization. As used in this definition, a "charitable organization" is an organization which exclusively, and in a manner consistent with existing laws and for the benefit of an indefinite number of persons, freely and voluntarily ministers to the physical, mental or spiritual needs of persons, and which thereby lessens the burdens of government~~ that has and maintains a current sales tax exemption certificate from the Colorado Department of Revenue.

Section 2. That Section 25-94(b) of the Code of the City of Fort Collins is hereby amended to read as follows:

(b) The application for an exempt organization license shall include copies of the organization's current certificate of incorporation and a copy of the institution's federal tax exemption letter, bylaws, and financial statements showing sources of funds, revenues and expenditures, and the organization's current sales tax exemption certificate from the Colorado Department of Revenue and, if the organization has been issued one, a copy of the Internal Revenue Service's letter of determination recognizing the organization as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code.

Section 3. That Section 25-241 of the Code of the City of Fort Collins is hereby amended by the addition of the defined term "charitable organization" to read as follows:

Charitable organization shall mean any entity that has and maintains a current sales tax exemption certificate from the Colorado Department of Revenue.

Section 4. That Section 25-243(2) of the Code of the City of Fort Collins is hereby amended to read as follows:

Sec. 25-243. Transactions exempt from tax.

“The following lodging transactions are exempt from taxation under this Article:

...

(2) All lodging accommodations provided to **religious, charitable organizations** and ~~eleemosynary corporations in the conduct of their religious, charitable and eleemosynary functions and activities only;~~ "

Introduced, considered favorably on first reading, and ordered published this 18th day of August, A.D. 2015, and to be presented for final passage on the 1st day of September, A.D. 2015.

Mayor

ATTEST:

City Clerk

Passed and adopted on final reading on the 1st day of September, A.D. 2015.

Mayor

ATTEST:

City Clerk