

**New York State Department of Taxation and Finance**  
**Office of Tax Policy Analysis**  
**Technical Services Division**

TSB-A-02(9)S  
Sales Tax  
May 31, 2002

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S010523A

On May 23, 2001, the Department of Taxation and Finance received a Petition for Advisory Opinion from Hilton Hotels Corporation, c/o Maria T. Jones, Esq., Kramer, Levin, Naftalis & Frankel, LLP, 919 Third Ave., New York, NY 10022.

The issue raised by Petitioner, Hilton Hotels Corporation, is whether costs incurred for the painting and installation of wall coverings in connection with the reconstruction of several floors in its hotel are exempt from the imposition of New York State sales and compensating use taxes as qualifying capital improvements under Sections 1101(b)(9) and 1105(c)(3)(iii) of the Tax Law.

Petitioner submitted the following facts as the basis for this Advisory Opinion.

Petitioner is the owner of a building located at 301 Park Avenue in New York City in which it operates a hotel known as The Waldorf Astoria. Petitioner has undertaken to reconstruct several floors of the hotel. Reconstruction requires the closure of the entire floor from use by the public. As a result, no revenue is generated for the duration of the construction period. The floor is out of service generally from 5 to 10 weeks. The reconstruction consists of the following.

During the demolition process, the contractor demolishes and removes any walls slated for demolition as determined by the architect and/or designer. Renovations in a few guest rooms include the removal of walls or parts of walls in order to accommodate new building code requirements with regard to accommodations for persons with disabilities. Occasionally, other walls are demolished for reasons consistent with Petitioner's use of the floor, for example, changes to service areas. Unnecessary demolition of walls is avoided as the walls are made of solid plaster and are difficult and expensive to remove and replace.

Wall and ceiling moldings are removed by the contractor in preparation for installation of new moldings. All existing electrical fixtures, devices and switches and selected outlets are removed for the installation of new devices. New wiring is installed wherever needed.

All walls are stripped to the base plaster. The contractor removes wall covering and paint of any type on the existing walls so that the bare surfaces of the plaster are exposed. In order to prepare the walls for new surfaces, all existing finishes and fixtures are stripped, leaving an "unfinished canvas." All walls, ceilings, soffits and fascias, including all vertical and horizontal surfaces, are then completely covered with a layer of new plaster. This process, the application of plaster via trowels, is called "skimming." After the new plaster is applied, all the surfaces are sanded. The process is time consuming and labor intensive.

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In conjunction with the skimming process, all existing metal surfaces (inclusive of but not limited to convector covers, grills in ceilings, doors and frames, etc.) are stripped. The stripping takes the metal "back to the bare metal" to allow a smooth application of new finishes. After the sanding of all plaster surfaces and the complete stripping of all metal surfaces, the surfaces are cleaned and prepared for the new finishes.

Paint is applied to all vertical and horizontal surfaces, inclusive of but not limited to moldings, chair rails, trims, doors and frames, convectors, and ceilings, all of which are physically and permanently attached to the building. All wall surfaces slated to receive wall covering receive an application of a special coating followed by the application of the wall covering.

During the demolition process, the contractor removes all existing carpeting, area rugs and carpet padding so that the building concrete floor slab is exposed. Damage to the concrete floor slab is corrected, if necessary. New padding and carpeting are installed on all floors. Floor tile is installed if appropriate.

Existing sink and other bathroom fixtures may be removed in preparation for the installation of new fixtures and other bathroom renovations.

The average cost of this building improvement is from \$2 million to \$3 million per floor, depending on how many guest rooms are on each floor. The cost of the project is capitalized for book purposes and tax purposes.

### **Applicable Law and Regulations**

Section 1101(b)(9)(i) of the Tax Law defines "capital improvement" as:

An addition or alteration to real property which:

(A) Substantially adds to the value of the real property, or appreciably prolongs the useful life of the real property; and

(B) Becomes part of the real property or is permanently affixed to the real property so that removal would cause material damage to the property or article itself; and

(C) Is intended to become a permanent installation.

\* \* \*

(iii) Notwithstanding the provisions of subparagraph (i) of this paragraph: (A) Floor covering, such as carpet, carpet padding, linoleum and vinyl roll flooring,

carpet tile, linoleum tile and vinyl tile, installed as the initial finished floor covering in new construction or a new addition to or total reconstruction of existing construction shall constitute an addition or capital improvement to real property, property or land; and

(B) Floor covering, such as carpet, carpet padding, linoleum and vinyl roll flooring, carpet tile, linoleum tile and vinyl tile, installed other than as described in clause (A) of this subparagraph shall not constitute an addition or capital improvement to real property, property or land.

Section 1105(c)(3)(iii) of the Tax Law provides an exclusion from tax “for installing property which, when installed, will constitute an addition or capital improvement to real property, property or land, as the terms real property, property or land are defined in the real property tax law as such term capital improvement is defined in paragraph nine of subdivision (b) of section eleven hundred one of this chapter.”

Section 527.7(b)(4) of the Sales and Use Tax Regulations provides, in part:

The imposition of tax on services performed on real property depends on the end result of such service. If the end result of the services is the repair or maintenance of real property, such services are taxable. If the end result of the same service is a capital improvement to the real property, such services are not taxable.

Section 541.14 of the Sales and Use Tax Regulations provides, in part:

**Floor Covering.** (a)(1) The installation of floor covering is subject to sales tax, regardless of the method of installation or the surface over which the floor covering is installed, unless the installation qualifies for exemption under subdivision (b) of this section.

(2)(i) The term floor covering includes carpet, carpet tile, carpet padding, linoleum and vinyl roll floor covering, linoleum tile, vinyl tile and other similar floor coverings but not area rugs and the like.

(ii) The term floor covering does not include flooring such as wood flooring, ceramic tile, terrazzo, marble, concrete or other similar flooring. Accordingly, the provisions of this section do not apply to the installation of flooring. See section 527.7 of this Title for the rules to determine whether such flooring qualifies as a capital improvement.

(b)(1) The installation of floor covering is exempt from sales tax only if the following criteria are met:

- (i) the installation must be of the initial finished floor covering; and
  - (ii) the installation must be made in:
    - (a) the new construction of a building or structure; or
    - (b) the new construction of an addition to an existing building or structure;
- or
- (c) the total reconstruction of an existing building or structure.
- (2) For purposes of this Subchapter:
- (i) "New construction of a building or structure" means the original construction of a building or structure that did not exist before such construction.
  - (ii) "New construction of an addition to an existing building or structure" means the original construction of a new room, wing or other discrete, substantial unit of a building or structure which enlarges the exterior of the existing building or structure.
  - (iii) "Total reconstruction of an existing building or structure" means the complete rehabilitation or replacement of most of the major structural elements of an existing building or structure, such as the roof, ceiling trusses, floor joists, walls, support columns, support beams, girders and the foundation.
- (3) Floor covering installed as the initial finished floor covering shall be deemed to be installed in new construction, a new addition or total reconstruction where it is installed within six months of the date of completion of the new construction, new addition or total reconstruction.

### **Opinion**

Petitioner owns and operates The Waldorf Astoria Hotel in New York City. Petitioner plans to reconstruct several floors of the hotel. The reconstruction project consists of the demolition of walls and parts of walls, replacing electrical and bathroom fixtures, stripping walls down to the base plaster, skimming, painting, installation of wall coverings, and replacing floor coverings, all at a cost of from \$2 million to \$3 million per floor.

These improvements substantially add to the value of the real property and their removal would cause damage to both the real property and to the items themselves. See Hodgson, Russ, Andrews, Woods & Goodyear, LLP, Adv Op Comm T&F, November 4, 1997, TSB-A-97(67)S.

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Where an owner of real property makes these kinds of improvements to the real property, the installation is presumably permanent in nature. See Matter of Flah's of Syracuse v. Tully, 89 AD2d 729. Accordingly, the remodeling of Petitioner's hotel floors, with the exception of the floor covering, meets the criteria set forth by Section 1101(b)(9) of the Tax Law for a capital improvement. See Maria T. Jones, Esq., Adv Op Comm T&F, December 30, 1998, TSB-A-98(91)S.

Where services such as painting and the installation of wall coverings are part of a major renovation project they must be viewed in the context of the entire project, in accordance with the "end result test" of Section 527.7(b)(4) of the Sales and Use Tax Regulations. See W P Owners Corp., Adv Op Comm T&F, March 17, 1997, TSB-A-97(13)S. Under the end result test, services performed on real property under a capital improvement project are treated as part of the project and are, therefore, not subject to sales tax. Accordingly, the contractor's charges to Petitioner for painting and for the installation of wall coverings that are performed as part of the reconstruction project are not subject to sales tax. See W P Owners Corp., *supra*; Maria T. Jones, Esq., *supra*.

The requirements for floor covering to become a capital improvement are statutorily different than other installations. See Section 1101(b)(9)(iii) of the Tax Law and Section 541.14 of the Sales and Use Tax Regulations. Petitioner's carpeting and other floor covering do not meet the criteria of such Sections 1101(b)(9)(iii) and 541.14 since they are not part of the new construction of a building or structure, an addition to an existing building or structure, or a total reconstruction of an existing building or structure. Therefore, charges to Petitioner for the installation of floor covering are subject to sales tax. See Maria T. Jones, Esq., *supra*; Hodgson, Russ, Andrews, Woods & Goodyear, *supra*. It should be noted that ceramic tile or marble is not floor covering for purposes of Section 1101(b)(9)(iii) of the Tax Law. See Section 541.14(a)(2) of the Sales and Use Tax Regulations. The installation of ceramic tile or marble as part of the remodeling described above would be considered part of the capital improvement and, therefore, not taxable.

DATED: May 31, 2002

/s/  
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NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.