

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

TSB-A-06(16)S
Sales Tax
May 30, 2006

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S050922B

On September 22, 2005, the Department of Taxation and Finance received a Petition for Advisory Opinion from Brookside Home Sales, Inc., 230 Route 17B, Monticello, New York, 12701. Petitioner, Brookside Home Sales, Inc., provided additional information pertaining to the Petition on January 4, 2006.

The issue raised by Petitioner is whether it must pay sales or compensating use tax on its purchases or collect tax on its sales of factory-manufactured homes (hereinafter "modular homes") as described below.

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

Petitioner is a dealer of mobile homes and a dealer/builder of modular homes constructed by a third-party manufacturer ("Manufacturer"). Petitioner advertises its relationship with Manufacturer to the general public. Petitioner maintains three locations with sales and support staff along with model modular homes for potential customers who are owners of real property (property owners) to view and inspect. Upon receiving an order for the purchase of an installed modular home from a property owner, Petitioner enters into a contract (hereinafter the "Customer Contract") with the property owner that provides for the sale and installation of a modular home to the property owner's specifications in exchange for a fixed purchase price. Petitioner provided copies of its standard Customer Contract with respect to its sales of modular homes. The agreement provides that Petitioner is obligated to provide the modular home, to deliver it to the property owner's building site, to install it on a foundation supplied by the property owner, and to apply the interior and exterior trim. The property owner typically pays Petitioner 20% of the purchase price upon execution of the Customer Contract, with the balance due upon delivery of the modular home components to the property owner's building site.

Upon the property owner's execution of Petitioner's Customer Contract with Petitioner providing for the sale and installation of a modular home, Petitioner orders the modular home components from Manufacturer. The specifications and purchase price of the modular home are outlined on an invoice issued to Petitioner by Manufacturer. Petitioner and Manufacturer enter into a Construction Service Contract in which Manufacturer has the contractual obligation to supply the modular home components to the property owner and to install those components on the property owner's building site. Among other things, the Construction Service Contract sets forth the fixed price to be paid by Petitioner to Manufacturer for the installation services rendered and itemizes the charges for the modular home components and options, freight, tax, carrier deposit, seals and inspections. Petitioner also provided a copy of its standard Construction Service Contract.

Manufacturer constructs the modular home components in its factory. In order to fulfill its obligation to install the modular home components on the property owner's foundation, Manufacturer enters into a Construction Service Subcontract with a subcontractor unrelated to Petitioner or Manufacturer in which the subcontractor contracts to install the modular home components on the property owner's site, i.e., to place and permanently affix the modular components on the property owner's foundation and bolt them together, apply the roof shingles, and install lolly (support) columns. Petitioner provided a copy of a standard Construction Service Subcontract. The Construction Service Subcontract provides that the Manufacturer will directly pay the subcontractor for the services supplied at an agreed-upon rate that is equivalent to the customary rate charged by other construction contractors for similar work.

Applicable law and regulations

Section 1101(b) of the Tax Law provides, in part:

When used in this article for the purposes of the taxes imposed by subdivisions (a), (b), (c) and (d) of section eleven hundred five and by section eleven hundred ten, the following terms shall mean:

(1) Purchase at retail. A purchase by any person for any purpose other than those set forth in clauses (A) and (B) of subparagraph (i) of paragraph (4) of this subdivision.

* * *

(4) Retail sale. (i) A sale of tangible personal property to any person for any purpose, other than (A) for resale as such or as a physical component part of tangible personal property, or (B) for use by that person in performing the services subject to tax under paragraphs (1), (2), (3), (5), (7) and (8) of subdivision (c) of section eleven hundred five where the property so sold becomes a physical component part of the property upon which the services are performed or where the property so sold is later actually transferred to the purchaser of the service in conjunction with the performance of the service subject to tax. Notwithstanding the preceding provisions of this subparagraph, a sale of any tangible personal property to a contractor, subcontractor or repairman for use or consumption in erecting structures or buildings, or building on, or otherwise adding to, altering, improving, maintaining, servicing or repairing real property, property or land, as the terms real property, property or land are defined in the real property tax law, is deemed to be a retail sale regardless of whether the tangible personal property is to be resold as such before it is so used or consumed, except that a sale of a new mobile home to a contractor, subcontractor or repairman who, in such capacity, installs such property is not a retail sale. . . .

* * *

(9) Capital improvement. (i) 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.

Section 1105 of the Tax Law provides, in part:

Imposition of sales tax On and after June first, nineteen hundred seventy-one, there is hereby imposed and there shall be paid a tax . . . upon:

(a) The receipts from every retail sale of tangible personal property, except as otherwise provided in this article.

* * *

(c) The receipts from every sale, except for resale, of the following services:

* * *

(3) Installing tangible personal property . . . or maintaining, servicing or repairing tangible personal property . . . except:

* * *

(iii) 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 1110 of the Tax Law provides, in part:

Imposition of compensating use tax (a) Except to the extent that property or services have already been or will be subject to the sales tax under this article, there is hereby imposed on every person a use tax for the use within this state on and after June first, nineteen hundred seventy-one except as otherwise exempted under this article, (A) of any tangible personal property purchased at retail, (B) of any tangible personal

property . . . manufactured, processed or assembled by the user, (i) if items of the same kind of tangible personal property are offered for sale by him in the regular course of business or (ii) if items are used as such or incorporated into a structure, building or real property by a contractor, subcontractor or repairman in erecting structures or buildings, or building on, or otherwise adding to, altering, improving, maintaining, servicing or repairing real property, property or land, as the terms real property, property or land are defined in the real property tax law, if items of the same kind are not offered for sale as such by such contractor, subcontractor or repairman or other user in the regular course of business, . . .

* * *

(c) For purposes of subclause (i) of clause (B) of subdivision (a) of this section, the tax shall be [computed on] the price at which items of the same kind of tangible personal property are offered for sale by the user, . . .

(d) For purposes of subclause (ii) of clause (B) of subdivision (a) of this section, the tax shall be [computed on] the consideration given or contracted to be given for the tangible personal property manufactured, processed or assembled into the tangible personal property the use of which is subject to tax, including any charges for shipping or delivery as described in paragraph three of subdivision (b) of section eleven hundred one.

Section 1115(a) of the Tax Law provides, in part:

Receipts from the following shall be exempt from the tax on retail sales imposed under subdivision (a) of section eleven hundred five and the compensating use tax imposed under section eleven hundred ten:

* * *

(17) Tangible personal property sold by a contractor, subcontractor or repairman to a person other than an organization described in subdivision (a) of section eleven hundred sixteen, for whom he is adding to, or improving real property, property or land by a capital improvement, or for whom he is about to do any of the foregoing, if such tangible personal property is to become an integral component part of such structure, building or real property; provided, however, that if such sale is made pursuant to a contract irrevocably entered into before September first, nineteen hundred sixty-nine, no exemption shall exist under this paragraph.

Section 1132(c)(1) of the Tax Law provides, in part:

For the purpose of the proper administration of this article and to prevent evasion of the tax hereby imposed, it shall be presumed that all receipts for property or services of

any type mentioned in subdivisions (a), (b), (c) and (d) of section eleven hundred five . . . are subject to tax until the contrary is established, and the burden of proving that any receipt . . . is not taxable hereunder shall be upon the person required to collect tax or the customer. Except as provided in subdivision (h) or (k) of this section, unless (i) a vendor, not later than ninety days after delivery of the property or the rendition of the service, shall have taken from the purchaser a resale or exemption certificate in such form as the commissioner may prescribe, signed by the purchaser and setting forth the purchaser's name and address and, except as otherwise provided by regulation of the commissioner, the number of the purchaser's certificate of authority, together with such other information as the commissioner may require, to the effect that the property or service was purchased for resale or for some use by reason of which the sale is exempt from tax under the provisions of section eleven hundred fifteen, and, where such resale or exemption certificate requires the inclusion of the purchaser's certificate of authority number or other identification number required by regulations of the commissioner, that the purchaser's certificate of authority has not been suspended or revoked and has not expired as provided in section eleven hundred thirty-four, or (ii) the purchaser, not later than ninety days after delivery of the property or the rendition of the service, furnishes to the vendor: any affidavit, statement or additional evidence, documentary or otherwise, which the commissioner may require demonstrating that the purchaser is an exempt organization described in section eleven hundred sixteen, the sale shall be deemed a taxable sale at retail. . . .

Section 541.2 of the Regulations provides, in part:

Definitions. The words, terms and phrases used in this Part have the following definitions except when the context clearly indicates a different meaning:

* * *

(d) A *construction contractor* means any person who engages in erecting, constructing, adding to, altering, improving, repairing, servicing, maintaining, demolishing or excavating any building or other structure, property, development, or other improvement on or to real property, property or land.

Section 541.5 of the Regulations provides, in part:

Contracts with customers other than exempt organizations.

* * *

(b) Capital improvements contracts. (1) Purchases. All purchases of tangible personal property (excluding qualifying production machinery and equipment exempt under section 1115(a)(12) of the Tax Law) which are incorporated into and become part

of the realty or are used or consumed in performing the contract are subject to tax at the time of purchase by the contractor or any other purchaser. A certificate of capital improvement may not be validly given by any person or accepted by a supplier to exempt the purchase of these materials.

(2) Labor and material charges. All charges by a contractor to the customer for adding to or improving real property by a capital improvement are not subject to tax provided the customer supplies the contractor with a properly completed certificate of capital improvement.

* * *

(4) Documents; capital improvement contracts. (i) When a properly completed certificate of capital improvement has been furnished to the contractor, the burden of proving the job or transaction is not taxable and the liability for the tax rests solely upon the customer.

(a) The prime contractor should obtain a certificate of capital improvement from the customer and retain it as part of his records. Copies of such certificate must be furnished to all subcontractors on the job and retained as part of their records.

(b) A certificate of capital improvement may not be issued by a contractor, subcontractor or any other person to a supplier on the purchase of tangible personal property.

Opinion

As a general matter, work performed on real property will qualify as a capital improvement to real property if all of the conditions set forth in section 1101(b)(9)(i) of the Tax Law are met. The installation of a permanent building or structure (including a modular home) for the owner of real property will qualify as a capital improvement to real property, and the prime contractor should not charge sales tax to the customer for building materials or labor on the capital improvement project. The prime contractor should obtain for its records a properly completed *Certificate of Capital Improvement* (Form ST-124) from its customer in order to be relieved of the burden of proving that the transaction is not subject to sales tax. See section 1132(c)(1) of the Tax Law. In order to be properly completed, a *Certificate of Capital Improvement* must contain all the information required on the form and must contain the name, address and *Certificate of Authority* number (if any) of the prime contractor. A contractor is considered to be the consumer of all building materials used in a capital improvement and generally must pay sales tax on the materials at the time of purchase. See section 541.5(b)(1) of the Sales and Use Tax Regulations. Sales tax paid by a contractor on building materials used in

a capital improvement may be included in the cost of materials and passed through to the customer.

As stated above, a contractor is considered the consumer of all building materials used in a capital improvement and generally must pay sales tax on the materials at the time of purchase. A contractor or subcontractor may not use a *Certificate of Capital Improvement* to purchase building materials or other tangible personal property tax free. A contractor's acceptance of this certificate does not relieve the contractor of its liability for sales tax on its purchases.

Since the contractor or subcontractor bears the liability for the sales tax on its purchases of building materials used in a capital improvement, the tax paid on those materials becomes the contractor's or subcontractor's expense, just as the price of the materials themselves are the contractor's or subcontractor's expense. The sales tax paid by a contractor or subcontractor on building materials used in a capital improvement may be included in the cost of materials and passed through to the customer, the same as any other expense is included in the contractor's or subcontractor's cost.

In the present case, Petitioner is a dealer of modular homes constructed and installed by Manufacturer. Petitioner enters into a Customer Contract with a property owner which provides for the sale and installation of a modular home. Accordingly, Petitioner is a construction contractor for sales tax purposes. See section 541.2(d) of the Sales and Use Tax Regulations. Even though Petitioner's Customer Contract, in part, may appear to be an agreement for the sale of tangible personal property, section 1115(a)(17) of the Tax Law exempts from sales tax the sale of building materials by a contractor or subcontractor to a person for whom the contractor or subcontractor is adding to or improving real property, property, or land by a capital improvement, provided that the tangible personal property is to become an integral component part of the structure, building or real property. Generally, the installation of a modular home qualifies as a capital improvement to real property. Thus, Petitioner's charges to the property owner for the sale and installation of a modular home are not subject to sales tax and the property owner should provide Petitioner with a properly completed *Certificate of Capital Improvement* (Form ST-124). Acceptance of this certificate by Petitioner in good faith relieves Petitioner of its obligation to collect sales tax from the property owner.

Petitioner has a subcontract (the Construction Service Contract) with Manufacturer that requires Manufacturer to provide and install a modular home. Therefore, Manufacturer is also considered a construction contractor pursuant to section 541.2(d) of the Sales and Use Tax Regulations. Assuming that the installation of the modular home qualifies as a capital improvement, Manufacturer's charges to Petitioner for materials to be installed by Manufacturer and installation services provided by Manufacturer are not subject to sales tax under sections 1105(c)(3)(iii) and 1115(a)(17) of the Tax Law. Petitioner should provide Manufacturer with a copy of the *Certificate of Capital Improvement* issued by the property owner. See section 541.5(b)(4)(a) of the Sales and Use Tax Regulations. Acceptance by Manufacturer in good faith of a properly completed *Certificate of Capital Improvement* relieves Manufacturer of its

obligation to collect sales tax from Petitioner on its charges for the provision of a modular home on an installed basis.

Manufacturer, in turn, executes a Construction Service Subcontract with another subcontractor to perform the installation services. It should be noted that whether such subcontractor is selected from a pre-approved list submitted by Manufacturer to Petitioner, directly by Petitioner, or by other means, the subcontractor is providing installation services to Manufacturer since the Construction Service Subcontract is executed between Manufacturer and the subcontractor. The subcontractor's charges to Manufacturer for installation services under the provisions of the Construction Service Subcontract are not subject to sales tax under section 1105(c)(3)(iii) of the Tax Law. Manufacturer should provide any of its subcontractors with a copy of the *Certificate of Capital Improvement* that it received from Petitioner. See section 541.5(b) of the Sales and Use Tax Regulations.

Manufacturer and any subcontractors are liable for sales or use tax on their purchases of materials used or consumed in the installation of the modular home. See section 541.5(b)(1) of the Sales and Use Tax Regulations. In addition, Manufacturer is liable for use tax, computed as provided in section 1110 of the Tax Law, on the modular home components that it sold permanently installed to Petitioner, and it may pass through the amount of this tax to Petitioner as one of its costs.

DATED: May 30, 2006

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