

THE POWER OF BEING UNDERSTOOD



CONSTRUCTION INDUSTRY SALES AND USE TAX SEMINAR (OHIO/MICHIGAN)

Presented to: Construction Financial Management
Association

February 17, 2022

Today's Agenda

- **General Sales and Use Tax Terminology for Contractors**
 - 1.) Construction Contractors
 - 2.) Sales Tax vs. Use Tax
 - 3.) Nexus
 - 4.) Real Property vs. Tangible Personal Property
 - 5.) Contractor or Subcontractor
 - 6.) Exemptions and Exclusions
 - 7.) Factors that can Affect Taxability
 - 8.) Contractor Classifications

Today's Agenda

- **Ohio Sales Tax for Construction Contractors**

- 1.) Real Property vs. Tangible Personal Property
- 2.) Business Fixtures
- 3.) Contractee Certification Process
 - a.) Exemption Forms
- 4.) Pollution Control Certification and Exemptions
- 5.) Materials Used out-of-state
- 6.) Sales and Use Tax Sourcing Rules
- 7.) Exemption Certificates
- 8.) Tools, Machinery, and Consumables
- 9.) Taxable Services
- 10.) Industry Specific Rules
 - Public Utilities
 - Energy Projects
 - Substations
- 11.) Relevant Court Cases

Today's Agenda

- **Michigan Sales Tax for Construction Contractors**

- 1.) Real Property vs. Tangible Personal Property

- 2.) Delivery Charges and Installation

- 2.) Statutory Exemptions

- 3.) Manufacturer/Contractors

- Use Tax Treatment

- Direct Labor

- Finished Goods Inventory Value

- Inventory

- Price List

- Publication

- Other Activities of Manufacturer/Contractors

Today's Agenda

- **Ohio Commercial Activities Tax (CAT)**
 - 1.) Basics of the Tax
 - 2.) Filing Methods
 - 3.) Tiered Rate Structure
 - 4.) Agency Exclusion

Today's Agenda

Best Practices – Audit Preparedness

- 1.) Project Bidding and Budgeting
- 2.) Invoicing
- 3.) Purchasing and Accounts Payable
- 4.) General Best Practice
- 5.) What Documentation is required?

GENERAL OVERVIEW

CONSTRUCTION
CONTRACTORS

Construction Contractors

- The taxation of construction contractors and fabricators is often surprising because of the unique rules applied by many jurisdictions and the increased emphasis on the self-assessment of use taxes.
- Construction contractors are generally considered the consumer of all items purchased in the performance of a contract, which includes **raw materials, tools, supplies and consumables**.
- As consumers are liable for the taxes associated with these items.
- Taxes are not passed directly to the customer, but are included as a set amount in the total price quoted.
- Like any other costs, the goal is to minimize sales and use taxes while maximizing profit.

Construction Contractors

- States vary in defining what is the taxable moment for contractors.
- Unique tax treatment of construction contractors can lead to unnecessary tax payments as well as subsequent interest and penalty charges upon later assessments.
- Other issues may also arise such as customer relation problems, if a state attempts to recoup additional amounts due, and the increased potential for audits in future years.

Construction Contractors

Manufacturer Contractors

- **Manufacturer**

- Manufacturers and contractors are taxed under different sales tax rules
- Manufacturer purchases industrial materials to be incorporated into product tax free and sales tax is collected at the retail sale level
- If a manufacturer withdraws materials from inventory, the manufacturer has to self assess sales/use tax based on the full fair market value of the property

Construction Contractors

Manufacturer Contractors

- **Contractor**

- In contrast, a contractor is always deemed to be the consumer of property used in a contract, even if furnished by the customer; accordingly, a contractor pays sales/use tax on materials and does not charge sales tax on contract price
- When company fabricate or manufacture products for sale to third parties as well as for their own use in contracting, the law can become very unsettled due to the mixing of the varying rules

SALES TAX VS. USE TAX

Sales Tax vs. Use Tax

- Sales and use tax are generally the same in that they both apply a percentage of tax on the price of a sale that is collected by a seller or assessed by a buyer and remitted to the state or local taxing authority.
- However, there are subtle differences in how each are collected and remitted.
- **Sales Tax:**
 - Tax on the sale, transfer, or exchange of a taxable item or service, at the time of sale. Sales tax is added to the price of the taxable item being purchased or taxable services being provided and charged to the consumer.
 - Businesses that have “nexus” (physical presence or have reached the threshold of economic transactions or sales in that state) must register to collect, charge the applicable sales tax, and remit it to the state.

Sales Tax vs. Use Tax

- **Example:**

- Company A purchases a new laptop computer for use in its Hinckley, Ohio office. The laptop cost \$1,000 (\$950 laptop plus \$50 shipping) and is purchased from an online retailer that does not have nexus in Ohio. Therefore, the seller does not charge Ohio sales tax.
- Since the out-of-state vendor did not collect sales tax and the laptop will be used in Hinckley, Ohio in a taxable manner, Company A should self-assess Ohio's consumers use tax.

Laptop \$950	State Rate	5.75%
<u>Freight \$50</u>	<u>County Rate</u>	<u>1.00%</u>
Total \$1,000	Combined	6.75%

Consumers use tax of \$67.50 is due to the Ohio Department of Revenue

NEXUS

Nexus

- **Nexus**: defines the level of connection between a taxing jurisdiction such as a state and an entity such as your business.
- Until this physical or economic connection is established, the taxing jurisdiction cannot impose its sales taxes on you.
- Nexus determination is primarily controlled by the U.S. Constitution, in which the **Due Process Clause** requires a **definite link or minimal connection** between a state and the entity it wants to tax, and the **Commerce Clause** requires **substantial presence**.

Nexus

- In *South Dakota v. Wayfair*, the Court **eliminated the physical presence rule within the Commerce Clause as the standard for creating nexus in a jurisdiction.**
- Economic nexus was a central issue in the United States Supreme Court case, [*South Dakota v. Wayfair*](#). On June 21, 2018, the U.S. Supreme Court ruled in favor of South Dakota and overruled the traditional physical presence rule as a necessary requirement to impose sales tax and collection requirements on a remote retailer.
- States now have the right to require tax collection from online retailers and other remote retailers with no physical presence in their state if they meet certain economic thresholds.
- Generally, over \$100,000 in sales and/or 200 transactions

Nexus

- However, physical presence will still create nexus and is the first consideration in determining nexus.
- Now in addition to physical presence there is economic nexus.

Each state has its own nexus guidelines.

- Having a physical presence in a state (permanent or temporary) usually suggests a substantial connection to a state. However, physical presence can be complicated because it can be created by third parties acting on a company's behalf.
- **Example:** The use of subcontractors is considered a physical presence for the general contractor in the state where the work is being performed.
- For contractors, if they have a job in a state, they most likely have nexus and a sales or use tax filing obligation.

REAL PROPERTY VS. TANGIBLE PERSONAL PROPERTY

Real Property vs. Tangible Personal Property

- **Real property vs. tangible personal property**
- Why do we care?
- We care because it determines:
 - Who pays tax?
 - Tax base used for calculating the tax owed
 - Necessary to account for sales/use tax in bid process to ensure accurate determination of bids and budget

Real Property vs. Tangible Personal Property

- **Real Property**
 - Contractor pays tax as the consumer
 - Contractor pays tax at material or produced cost

- **Tangible Personal Property**
 - Contractee pays tax as the consumer
 - Contractee pays tax on the marked-up price from the contractor which includes installation labor

Real Property vs. Tangible Personal Property

- **In general:**

- When is a contractor considered to be constructing, altering, repairing or improving real property?

- **Three primary tests:**

- 1.) Intent of parties

- Intended to become permanent installation

- 2.) Degree of affixation

- Becomes part of real property or is permanently affixed to real property so that removal would cause material damage to the property or article itself

- Ohio differs, we will cover later (Business Fixtures)

- 3.) Substantially adds to the value of or prolongs the useful life of the real property

- Alternatively, specific to current occupant and not to realty

CONTRACTOR OR SUBCONTRACTOR

Contractor or Subcontractor

- Depending on how big a job is, you may be working as either a "prime contractor" or a "sub-contractor."
- Being the prime contractor on a large construction job means that you will contract with a customer to perform all the work on a construction job and bill this customer for the entire amount of the job.
- As a subcontractor, however, you will be hired by the prime contractor and have little, if any, contact with the customer.
- The payment you receive will typically come from the prime contractor.
- However, you'll still be treated like an end consumer and have to pay sales and use taxes when you purchase supplies and materials.

Contractor or Subcontractor

- **Construction Contractors**

- Prime, Subcontractor or U.S. Contractor**

- **Prime Contractors** — The contractor that has a contract with the owner of a project or job and has the full responsibility for its completion. A prime contractor undertakes tasks to perform a complete contract and may employ (and manage) one or more subcontractors to carry out specific parts of the contract.
 - **Subcontractors** — A subcontractor is an individual or business contracting to perform part or all of another's contract. In general, most contractors do some of the work themselves and use subcontractors for the rest
 - **United States Construction Contractors** — A United States construction contractor is a construction contractor who performs a construction contract for the United States government

EXEMPTIONS AND EXCLUSIONS

Exemptions and Exclusions

Exempt Projects and Organizations

- General Multistate Examples
 - Nonprofit Hospitals
 - Inurement of Benefit Test
 - Qualified Nonprofit Housing
 - Church Sanctuaries
 - Qualified Water or Air Pollution Control Facilities
 - Public Utility
 - Manufacturer
 - Pollution Control Exemption
 - Qualified Convention Facilities, Data Centers
 - State/Tribal Tax Agreements
 - Qualified Business Activities (enterprise zones)
 - Foundations for Certain Machinery or Equipment Used in Industrial Processing
 - Property to be Affixed to and Becoming a Structural Part of Real Estate
 - Materials for use in another state

Exemptions and Exclusions

Exempt Organizations

- Many times, but not all, the exemption flows from the exempt entities to the contractor and subcontractor
- Generally the exemption applies only to Limited portion of the facility
- Documentation needed to support the exemption may vary depending on the facility.
 - Pollution control
 - Non-profit hospital
 - Government contact

FACTORS THAT CAN AFFECT TAXABILITY

Factors that can Impact Taxability

Examples (Not all inclusive)

- **Customer Type**
 - Exempt entity
 - Government
 - Non-profit
- **Project Type**
 - Research and Development
 - Port authority projects
 - Pollution control
- **Type of contract and invoicing**
 - Form over Substance
 - How the contractor invoices the contractee
 - Lump sum
 - Materials and labor charged for single price
 - Time and materials
 - Material and labor charged separately

CONTRACTOR CLASSIFICATIONS

Contractor Classifications

- **Three Categories of Contractors**

1.) Real Property Contractor – constructing, altering, repairing or improving real estate by affixing tangible personal property a structural part of real property

- Consumer of tangible personal property
 - Contractor pays sales tax to vendor OR
 - Contractor pays use tax on property consumed
- **Examples:**
 - Retailer sells property and installation, hires contractor = Retailer Responsible Contractor is not responsible for use tax on installation
 - Contractor obtains property from third party non-retailer where tax was not paid Contractor is responsible for use tax on installation

Contractor Classifications

Three Categories of Contractors

2.) Real Property Contractor acting as Retailer – contractor consistently acts as retailer and collects tax consistently

Collect sales tax on the sales of tangible personal property

- Collect sales tax on retail sale price, price must be equal to or exceed the cost of materials
- Examples:
 - a. Property remains tangible personal property such as subsurface agricultural drainage systems, land tile, and portable grain bins installed by contractor
 - b. Contractor does not normally make retail sales may be treated as retailer – For example - agricultural projects.
 - a. A contractor that does not usually make retail sales may be treated as a retailer in certain transactions with an agricultural producer. A resale sales/use tax exemption applies to the contractor's purchase. An agricultural exemption may be claimed upon installation or transfer to the agricultural producer because the contractor is not the end user of tangible personal property

Contractor Classifications

- **Three Categories of Contractors**

- 3.) **Manufacturer Contractor** – person that does BOTH:

- Manufactures, fabricates and or assembles tangible personal property AND
 - Affixes tangible personal property to real estate for others
 - Sales Tax - Retail sales are subject to sales tax on the full sale price
 - Use Tax – depends on if inventory offered for sale to public (Michigan)
 - Examples:
 - Manufacturer Contractor - maintains an inventory of its items available for sale to others
 - Use tax base for items withdrawn from inventory and affixed to realty is finished goods inventory value

Contractor Classifications

Move to Michigan Inventory-Manufacturer Contractors (Affixes its Product to Real Estate)

- **Maintaining an Inventory** of manufactured products available for sale to others Direct production costs and indirect production costs of the product affixed to the real estate that are incident to and necessary for production or manufacturing operations or processes are subject to sales and use tax.
- **Not Maintaining an Inventory** of its product available for sale to others or make its product available for sale to others Materials cost of the property and the cost of labor to manufacture, fabricate, or assemble the property affixed to real estate in Michigan, is subject to sales and use tax.

Contraction Project Types

Factors that affect the taxability of your transactions include:

- **Project category — Commercial or residential**
 - Commercial real estate is defined as buildings or land that is intended to generate a profit from capital gain or rental income.
 - Residential projects are buildings designed primarily to be dwellings
- **Construction Type — New, repair or maintenance**
 - New construction — Entirely new structures and/or significant extensions to existing structures, whether or not the site was previously occupied.
 - Repair — A restoration to return a structure or property to operating or usable condition.
 - Maintenance — Making or keeping a structure, fixture, or foundation (substrates) in proper condition in a routine, scheduled, or anticipated fashion

Contractor Classifications

Project Types

- **Lump Sum** - project in which the agreed-upon contract price is one lump-sum amount. The charges for materials are built right into the job and are not separate from the charges for labor.
- **Separated or Time and Materials Contracts** – project in which the agreed-upon contract price is divided into separately stated agreed upon prices one for materials and one for labor.
- **Cost-Plus Contracts** - A cost-plus contract is used when the contractor is paid for all allowed expenses plus additional payment to allow for a profit to be made.

OHIO

CONSTRUCTION
CONTRACTORS

OHIO

REAL PROPERTY VS.
TANGIBLE PERSONAL
PROPERTY

Ohio - Real Property vs. Tangible Personal Property

- **Real Property vs. Tangible Personal Property**
 - R.C. 5739.01(B)(5) – a “sale” does not include “a construction contract in which tangible personal property is incorporated into a structure or improvement on and becoming real property”
 - A construction contractor is the consumer of all tangible personal property incorporated into realty as part of a construction contract

Ohio - Real Property vs. Tangible Personal Property

- Ohio Revenue Rule 5703-9-14 covers construction contracts and exemption certificates
 - Generally, contractors do not collect sales tax from their customers on the performance of a real property construction contract. For real property jobs, the contractor is considered the consumer of the materials installed and must pay sales or use tax at the time the materials are purchased.
 - In contrast, if a contractor is installing a **“business fixture”** the item does not become part of real property for Ohio sales tax purposes, even though it may be permanently affixed to real property. The items being installed remain tangible personal property. Thus, the contractor must collect sales tax from the customer.

Ohio - Real Property vs. Tangible Personal Property

- ***Real Property vs. Tangible Personal Property***

Real Property

- R.C. 5701.02 – Land and, unless otherwise specified, buildings, structures, improvements, and fixtures on the land

Tangible Personal Property

- R.C. 5701.03 (A) – Every tangible thing that is the subject of ownership and is not real property

Business Fixture

- R.C. 5701.03(B) – An item of tangible personal property that is permanently affixed to realty and that primarily benefits the business conducted on the premises and not the realty

Ohio - Real Property vs. Tangible Personal Property

- ***Real Property vs. Tangible Personal Property***
- **Real Property**
 - Contractor pays tax as the consumer
 - Contractor pays tax at material or produced cost
- **Tangible Personal Property**
 - Contractee pays tax as the consumer
 - Contractee pays tax on the marked-up price from the contractor which includes installation labor

Ohio - Real Property vs. Tangible Personal Property

- **Business Fixture**
- **5701.03 Personal property and business fixture defined.**
- (A) "Personal property" includes every tangible thing that is the subject of ownership, whether animate or inanimate, including a business fixture, and that does not constitute real property as defined in section 5701.02 of the Revised Code. "Personal property" also includes every share, portion, right, or interest, either legal or equitable, in and to every ship, vessel, or boat, used or designed to be used in business either exclusively or partially in navigating any of the waters within or bordering on this state, whether such ship, vessel, or boat is within the jurisdiction of this state or elsewhere. "Personal property" does not include money as defined in section 5701.04 of the Revised Code, motor vehicles registered by the owner thereof, electricity, or, for purposes of any tax levied on personal property, patterns, jigs, dies, or drawings that are held for use and not for sale in the ordinary course of business, except to the extent that the value of the electricity, patterns, jigs, dies, or drawings is included in the valuation of inventory produced for sale.

Ohio - Real Property vs. Tangible Personal Property

- **Business Fixture**

- **5701.03 Personal property and business fixture defined.**

- (B) "Business fixture" means an item of tangible personal property that has become permanently attached or affixed to the land or to a building, structure, or improvement, and that primarily benefits the business conducted by the occupant on the premises and not the realty. "Business fixture" includes, but is not limited to, machinery, equipment, signs, storage bins and tanks, whether above or below ground, and broadcasting, transportation, transmission, and distribution systems, whether above or below ground. "Business fixture" also means those portions of buildings, structures, and improvements that are specially designed, constructed, and used for the business conducted in the building, structure, or improvement, including, but not limited to, foundations and supports for machinery and equipment. "Business fixture" **does not** include fixtures that are common to buildings, including, but not limited to, heating, ventilation, and air conditioning systems primarily used to control the environment for people or animals, tanks, towers, and lines for potable water or water for fire control, electrical and communication lines, and other fixtures that primarily benefit the realty and not the business conducted by the occupant on the premises.

Ohio - Real Property vs. Tangible Personal Property

Real Property vs. Tangible Personal Property

- Items Never Treated as Construction Contract Under R.C. 5739.01(B)(5) and O.A.C. 5703-9-14(C):
 - Carpeting
 - Landscaping and lawn care services
 - Agricultural land tile
 - Grain bin
- Examples of Items Treated as Business Fixtures:
 - Gas station canopies
 - Security cameras that protect inventory of interior rooms
 - HVAC and flooring for computer rooms
 - Specialty lighting/parking lot lighting at car dealerships
 - Window treatments
 - Specialty cabinetry

Ohio Information Release 2007-01 lists additional items properly classified as tangible personal property.

Real Property vs. Tangible Personal Property

- **Real property vs. tangible personal property determination impacts:**
 - Who pays tax?
 - Tax base used for calculating the tax owed
 - Accurate determination of bids and project budget

Ohio - Real Property vs. Tangible Personal Property

- **So what does all of that mean?**
 - Before starting a job, the contractor **MUST** determine if they are selling a business fixture or selling real property.
 - This determination is **imperative** in order to determine proper sales tax treatment.
 - Following are some examples of some items that retain their status as tangible personal property “business fixture” vs. real property.

OHIO

BUSINESS FIXTURES

Ohio - Business Fixtures

- **Business Fixtures**

- Unique property classification rules for Ohio
 - Making the determination between real property and business fixtures is not an easy undertaking.
 - The key in making the accurate determination is to look at whether the project increases or enhances the utilization or enjoyment of the land, or whether the property primarily benefits the business conducted on the premises
- So, as you can see it is clear as mud. Thus, there are many Ohio court cases on the distinction between real property and business fixtures

Ohio - Business Fixtures

- **Case Law**

- ***Funtime, Inc. v. Wilkins*, 105 Ohio St.3d 74**

- The Ohio Supreme Court determined that amusement park rides are business fixtures and not real property. During an audit, the Ohio Department of Taxation (ODT) taxed the installation of the rides as tangible personal property. Funtime argued that the rides were real property and the contractor was responsible to pay sales tax on the materials. The court ruled in favor of ODT.

- ***Metamora Elevator Co. v. Fulton Cty. Bd. of Revision*, 143 Ohio St.3d 359 (2015)**

- Affirming *Funtime* analysis and holding that grain storage bins are business fixtures under the plain language of R.C. 5701.03

Case Law

Nationwide Mutual Insurance Company v. McClain

BTA Cases: 2018-313, 2018-315, 2018-316, 2018-317, 2018-318

- Applicability of business fixture concept to computer cabling
- Standard CAT-5/CAT-6 VoIP and Internet cabling, argued cabling is common to buildings and is a real property contract
- ODT previously relied on 1998 BTA case, *Newcome Corp. v. Tracy*
- Computer cabling always treated as business fixture
- Telephone (communication) lines were real property
- Court considered the following:
 - Cabling was not designed to meet the specific business requirements of Nationwide
 - “As common to commercial property as telephone lines and coaxial cables were in the past”
 - Court determined cabling was real property

Case Law

Nationwide Mutual Insurance Company v. McClain **(cont.)**

- ODT did not appeal to the Supreme Court of Ohio
- ODT's position is applicability limited to specific types of cabling in case – CAT-5 and CAT-6
- Does not apply to fiber optic cable, even if used for oIP/internet in the same installation as CAT-5 or CAT-6
- If not subject to sales tax, contractor should have paid sales tax on purchase of cabling
- Impact to contractors for refund claims filed by building owners
- Work with cabling contractor to determine taxability of projects
- Potential use of contractee certification

Case Law

F. P. & E., Inc. vs. Tracy, Ohio BTA No. 96-M-806

- BTA found service station canopies were tangible personal property

Oregon Ford, Inc. v. Wilkins, Ohio BTA No. 2005-A-111

- Personal property tax case
- Parking lot lighting used to illuminate inventory was tangible personal property

Ohio - Business Fixtures

Always treated as Business Fixtures(Tangible Personal Property)

- Gas station canopies
- Security cameras to monitor inventory or interior rooms
- HVAC and special purpose flooring for computer rooms
- Lighting for parking lots at car dealerships
- **Certain computer cabling**
- Specialty indoor and outdoor lighting
- Special security door locking mechanisms for interior doors
- Window treatments
- Specialty cabinetry
- Sale and installation of carpeting
- Sale and installation of agricultural land tiles
- Sale and installation of portable grain bins
- Sale of landscaping services – including tree plantings and shrubs
- Signage
- Golf course irrigation systems
 - Foundations and pits for machinery
 - Amusement park rides
 - Indoor pool

Ohio - Business Fixtures

Business Fixture Examples

- **Examples of business fixtures in the following industries:**
 - **Golf courses** – drainage and irrigation systems are considered business fixtures and retain their status as tangible property after being affixed to real property and are therefore taxable. However, cart paths, bridges and catch basins are considered real property, and a contract to install these items is considered to be a construction contract.
 - **Manufacturing** – foundations for manufacturing equipment, fencing around manufacturing equipment for the protection of workers, and air conditioning systems that maintain specific environmental conditions in a limited area of the plant for manufacturing to occur are all examples of business fixtures. The entire charge would be taxable to the manufacturer, unless a specific exemption exists.
 - **Construction contracting** – items temporarily affixed during construction, even if they remain after construction is completed, retain their status as tangible property and are taxable. Examples of such business fixtures include temporary electricity, fencing, shoring lumber and concrete forms.

Ohio - Business Fixtures

Real Property

- Amphitheaters
- General parking lot lighting
- Tile, wood, and laminate flooring
- Refinished flooring
- Outdoor pool
- Dock doors/levelers
- Permanent Fencing
- Alarm systems to prevent entry from exterior
- Card reader on exterior door
- Security cameras on exterior
- Elevators

Ohio - Business Fixtures

Temporary Components - Ohio Admin. Code 5703-9-14

- Tangible personal property that is “temporarily” affixed or used during construction
- Applies even if items remain/become permanently affixed after construction because of forgetfulness, convenience, or economic preference
- **Examples**
 - Electricity/lighting (e.g., temporary tradeshow electric)
 - Water service
 - Protective fencing
 - Construction elevators
 - Shoring lumber
 - Concrete forms
 - Scaffolding
 - Stop lights/signage not incorporated into real property

Ohio - Business Fixtures

- **Special Circumstances**

- The sale and installation of the following items is never a construction contract and such transactions are to be treated as the sale and installation of tangible personal property for sales tax purposes:

- Carpeting, including carpet padding, tack strips, adhesive, and similar materials that are integral and necessary components of a carpet installation transaction
 - Agricultural land tile as defined in division (B)(5)(a) of section 5739.01 of the Revised Code
 - Portable grain bins as defined in division (B)(5)(b) of section 5739.01 of the Revised Code
 - Trees, shrubs, sod, seed, fertilizer, mulch, and other tangible personal property transferred as part of a landscaping and lawn care service as defined in division (DD) of section 5739.01 of the Revised Code.

Ohio - Business Fixtures

Selling a Business Fixture

The sale and installation of a business fixture is a retail sale, not a construction contract. Even though permanently attached, a business fixture is not deemed real property. The transaction is defined as the sale and installation of tangible personal property.

Contractor charges sales tax to the contractee / property owner on total contract amount.

All costs including the cost of material, labor, and mark-up must be included in the taxable price. Materials Are Purchased Tax Free for Resale by Contractor

Sales tax is calculated on the total cost (taxable base) of the business fixture sold. The construction contractor needs to maintain a regular county vendor's license; or if located out-of- state, a seller's use account.

Selling Real Property

The incorporation of materials (TPP) into realty, such as; building walls, painting a room, paving a parking lot, etc, that benefits the realty is a construction contract. The contractor is the "consumer" of the TPP installed into real property.

As there is no retail sale, no tax is collected from the contractee / property owner

Contractor **pays tax on materials**, does not collect tax from customer.

The construction contractor must pay sales tax on the materials purchased and incorporated into real property. If the material vendor does not collect sales tax, the contractor must accrue the use tax and remit to the state on a consumer's use tax.

Ohio - Business Fixtures

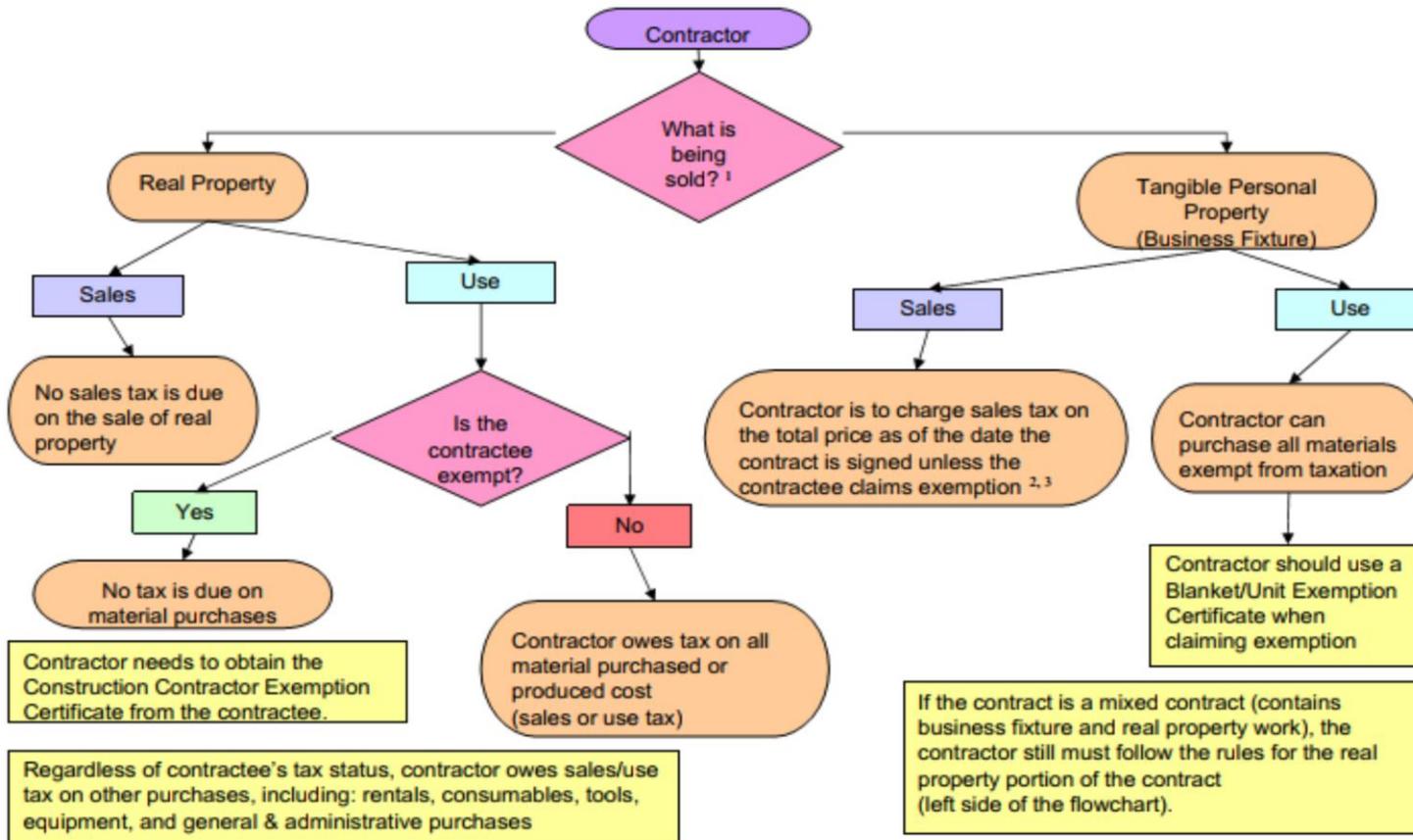
Business Fixture

Material Cost*	\$10,000
*(Materials purchased tax exempt under the resale exception)	
Labor Cost	\$5,000
Permit Fees	<u>\$500</u>
Subtotal	\$15,500
Sales Tax (15,500 * 7.5%)	\$1,162.50
Total	\$16,662.50

Real Property

Material Cost*	\$10,750
*(Includes sales tax paid to vendor or use tax accrued) (\$10,000 x 7.5%)	
Labor Cost	\$5,000
Permit Fees	<u>\$500</u>
Subtotal	\$16,250
Sales Tax	\$0
Total	\$16,250

Ohio - Business Fixtures



¹ – Contractor may request the contractee to complete the Contractee Certification Form if tangible personal property is being sold.

² – Contractor is to remit this sales tax on a regular county vendor's license.

³ – No matter if the contractor is an in-state or out-of-state contractor, sales tax is to be charged when the contract is signed; not when draws are made.

Ohio - Business Fixtures

Business Fixture Examples

A contractor installs temporary pavement to maintain traffic at a highway construction site. The contractor removes the temporary pavement at the end of the project.

- Is the temporary pavement taxable?
- If so, what is the tax base?

Ohio - Business Fixtures

Business Fixture Examples

A contractor installs temporary pavement to maintain traffic at a highway construction site. The contractor removes the temporary pavement at the end of the project.

- Is the temporary pavement taxable? **Yes, the temporary pavement is taxable even if the contractor did not remove the temporary pavement because it was “consumed” by the contractor in the performance of its project.**
- If so, what is the tax base? **The tax base would be the contractors’ cost of materials, including labor and installation.**

Ohio - Business Fixtures

Business Fixture Examples

A contractor hires a subcontractor to install temporary pavement to maintain traffic at a highway construction site. The temporary pavement is removed at the end of the project.

- Is the temporary pavement taxable to the contractor?
- If so, what is the tax base?

Ohio - Business Fixtures

Business Fixture Examples

A contractor hires a subcontractor to install temporary pavement to maintain traffic at a highway construction site. The temporary pavement is removed at the end of the project.

- Is the temporary pavement taxable to the contractor? **No. The contractor is not responsible. However, like the previous example the subcontractor would be responsible.** The temporary pavement is taxable even if the contractor did not remove the temporary pavement because it was “consumed” by the contractor in the performance of its project.
- If so, what is the tax base? **Same as the previous example. Instead of being taxable to the contractor it would be taxable to the subcontractor. The tax base would be the contractors’ cost of materials, including labor and installation.**

Ohio - Business Fixtures

Business Fixture Examples

The contractor hires a private security company to protect its equipment and materials on the highway construction site.

- Is this taxable?

Instead of a private security company, the contractor contracts with the local police for an off-duty officer to provide security.

- Is this taxable?

Ohio - Business Fixtures

Business Fixture Examples

The contractor hires a private security company to protect its equipment and materials on the highway construction site.

- Is this taxable? **Yes, the private security services are an enumerated taxable service.**

Instead of a private security company, the contractor contracts with the local police for an off-duty officer to provide security.

- Is this taxable? **No, Ohio has a specific exclusion from the private security service in that “peace officers” are not included in the definition of security services.**

OHIO
CONTRACTEE
CERTIFICATION
PROCESS
EXEMPTION FORMS

Ohio - Contractee Certification Process and Exemption Forms

- **Mixed Contracts – Certification Process**

- Ideally, the customer/contractee should issue a certification Contractee (Customer) Certification of Property Type to the contractor specifying which portion of the project is “real property” vs. “business fixture”, TPP
- Certification will determine if the contractor is either a consumer of materials purchased for a job, or the reseller of materials purchased for a job.
- For the business fixture portion, contractors should issue Certificates of Exemption to suppliers claiming “resale” as the basis for exemption
- Contractors with Direct Pay Permits should not accrue tax on business fixture portion
- Contractor should charge sales tax on the total price of business fixture portion including the cost of materials, labor, and mark-up unless contractee provides an exemption certificate or direct pay number.

Ohio - Contractee Certification Process and Exemption Forms

- **Construction Contracts with Exempt Entities**
- Even if the contract is exempt, the contractor is still liable for taxes on property not incorporated into real property improvements, such as tools, equipment and consumables.
- There is no specific form that I am aware of, but the rules indicate that the certificate **MUST** contain the following:
 - Contractee (owner's) name
 - Location of project
 - Name of project
 - Reason for exemption indicated
 - Name, signature, address and date signed by contractor and contractee

Ohio - Contractee Certification Process and Exemption Forms

- **Construction Contracts with Exempt Entities**
- **FORM STEC-CC – Sales and Use Tax, Construction Contract Exemption Certificate**
 - When contractors enter into a construction contract with an exempt entity it MUST be supported by the contractor’s receipt of an exemption certificate. The contractor should obtain a “Sales and Use Tax Construction Contract Exemption Certificate” (**Form STEC CC**) from the customer property owner.
 - This certificate may be used when making purchases of materials to be incorporated into real property as part of an exempt construction contract.
 - It must be signed by the contractor and/or subcontractor and by the political subdivision or other exempt contractee.
 - The contractor should retain the original of this certificate in the records of the exempt contract and provide copies to any supplies from whom purchases of construction materials are made.
 - **A contractor that provides a Construction Contract Exemption Certificate signed by the contractee is protected from liability if it is later determined that the contract did not qualify for exemption. In such a case, the contractee will assume the liability for any unpaid taxes.**

Ohio - Contractee Certification Process and Exemption Forms

- **Construction Contracts with Exempt Entities**
- Then, the contractor should provide “Sales and Use Tax Contractor’s Exemption” certificates ([Form STEC CO](#)) to its suppliers. O.A.C. § 5703-9-14(I).
- This certificate may be used when making purchases of materials to be incorporated into real property as part of an exempt construction contract.
- Unlike the Construction Contract Exemption Certificate, it is signed only by the contractor or subcontractor that is making the purchases of materials.
- Unlike the Construction Contract Exemption Certificate, this certificate protects only the vendor or seller and provides no protection to the contractor on audit.

Ohio - Contractee Certification Process and Exemption Forms

- Construction Contract Exemption Certificate.
- This certificate may be used when making purchases of materials to be incorporated into real property as part of an exempt construction contract.
- Signed by the contractor and/or subcontractor and by the political subdivision or other exempt contractee.
- Contractor should retain the original of this certificate in the records of the exempt contract and provide copies to any supplies from whom purchases of construction materials are made.
- Contractor that provides a Construction Contract Exemption Certificate signed by the contractee is protected from liability if it is later determined that the contract did not qualify for exemption.
- In such a case, the contractee will assume the liability for any unpaid taxes.

Ohio - Contractee Certification Process and Exemption Forms

- Contractor's Exemption Certificate.
- Certificate may be used when making purchases of materials to be incorporated into real property as part of an exempt construction contract.
- Unlike the Construction Contract Exemption Certificate, it is signed only by the contractor or subcontractor that is making the purchases of materials.
- Unlike the Construction Contract Exemption Certificate, this certificate protects only the vendor or seller and provides no protection to the contractor on audit.

OHIO POLLUTION CONTROL

Ohio - Pollution Control Exemptions

- The air and noise pollution control tax exemption program was originally established by legislation in 1963. The program allows companies to receive tax exemptions for the installation of air or noise pollution control property and is administered by the Ohio Department of Taxation and provides a sales and property tax exemption for the installation of air, water or noise pollution control property.
- As part of the tax exemption application process, Ohio EPA is required to provide a technical evaluation and review of any property sought for tax exemption status.

Ohio - Pollution Control Exemptions

- Specifically, the program (1) exempts the tangible personal property that will be incorporated into the facility from sales and use tax and (2) exempts the qualified property improvements from property tax.
- To obtain this exemption, the business must submit an application to the Department of Taxation containing plans and specifications of the property, including all materials incorporated or to be incorporated therein and their associated costs, and a descriptive list of all equipment acquired or to be acquired by the applicant for the exempt facility and its associated cost.
- The tax commissioner requests the review and approval of the Ohio EPA or Department of Natural Resources, which will then issue a recommendation to the tax commissioner regarding its findings.

Ohio - Pollution Control Exemptions

- After receiving a recommendation from the Ohio EPA or Department of Natural Resources regarding the project, the tax commissioner reviews the application to ensure that the facility is designed primarily for an exempt purpose and then grants or denies the exemption.
- If the exemption certificate is granted, all future purchases of property to be incorporated into the facility will be exempt from sales and use tax.
- There is a four-year statute of limitations to claim a refund for previously overpaid sales tax. Such sales tax refund claims can result in substantial savings.

Ohio - Pollution Control Exemptions

Practical Note:

- The certification process in Ohio requires that the pollution control facility be completed before it can be certified as an exempt pollution control facility by the Department and EPA.
- This causes a timing issue since the pollution control facility owner does not have a valid exemption certificate to issue to the contractor the during the building of the pollution control facility.
- The question then becomes: Can a contractor accept a blanket exemption certificate stating that the project is in the process of being certified?
- The Department's position on this is that you pay the tax then apply for a refund.

OHIO

MATERIALS USED OUT
OF STATE

Ohio - Materials Used out of State

- **Materials used out-of-state (Not Ohio)**

- Building and construction materials sold to a construction contractor for incorporation into real property outside this state are not subject to Ohio sales or use tax **if the materials would be exempt from tax when sold to the contractor in the other state.**
- The contractor's exemption does not apply to tools, equipment, rentals of personal property, form lumber, temporary items such as fencing, lighting, etc., and any other purchases of tangible personal property or taxable services, not incorporated into real property.

OHIO

SALES AND USE TAX
SOURCING RULES

OHIO - SALES AND USE TAX SOURCING RULES

Sourcing Sales

- Sourcing does not determine taxability of the sale or, in the case of an out-of-state seller, whether the seller has nexus and is required to collect Ohio tax. The purpose of sourcing is to determine the location of the sale for sales tax purposes.
- If a sale is taxable, the sourcing of the sale will determine the appropriate jurisdiction's tax rate for the seller to charge.
- Ohio vendors of tangible personal property will source their sales to Ohio consumers to the location where the vendors receive the order from the consumer.
- Vendors that make sales in Ohio, but do not make sales from a fixed location (e.g., transient vendors) will continue to source each sale to the location where the sale takes place.
- For remote sales (e.g., mail order, telephone or online sales) made by Ohio vendors to Ohio consumers, the sale will be sourced to the location where the order is received. Note the sourcing is based on where the order is received, which is not necessarily the location from which orders are processed or shipped.

OHIO - SALES AND USE TAX SOURCING RULES

Sourcing Sales

- If the order is received at a location outside Ohio, or the vendor does not capture the location where the order is received, the sale is treated as a sale from outside Ohio and sourced as noted below.
- Sales made by Ohio vendors that the vendor sends or delivers to non-Ohio customers will continue to be treated as sales in interstate commerce and not subject to Ohio tax. However, vendors should check with the states into which they ship to determine if they are required to collect tax for those states.
- Sales by out-of-state sellers to Ohio consumers will be sourced to the location where the consumer receives the tangible personal property that was sold. If this is not known to the seller, the seller should use an address of the consumer available from the seller's business records.

OHIO - SALES AND USE TAX SOURCING RULES

Providers of Services

- Sales of services should be sourced to the location where the consumer receives the service.
- Under Ohio law, a service is “received” where the customer makes first use of the service. While this may be somewhat new terminology, it should be little change for most service providers.
- For example, repair services should be sourced to the location where the consumer gets possession of the repaired object.
- Data processing services will continue to be sourced to the location of the consumer where the service is received.
- Exterminating service would continue to be sourced to the location where the eradication of vermin takes place.
- Recreation and sport club memberships would continue to be sourced to the location of the club where the member makes use of the membership privileges.
- For sourcing purposes, it does not matter whether the provider of the service is located in Ohio or outside Ohio. The relevant issue is where the consumer receives the service.

OHIO - SALES AND USE TAX SOURCING RULES

Leases of Tangible Personal Property

- Generally, leases are sourced to the primary location of the property at the time the tax is to be paid. However, there are variations, [which are noted on the attached sourcing chart.](#)

Consumers

- Consumers that purchase tangible personal property, and who remit Ohio sales tax to the seller at either the rate applicable where the order was received or where the consumer received the tangible personal property, will not be liable for any additional Ohio sales or use tax on that transaction. This eases the burden on consumers by eliminating the requirement that they determine additional use tax on transactions where the vendor has sourced the sale to its location.

The provisions of the above paragraph apply only to sales of tangible personal property.

- For sales of services, consumers must remit use tax based on the location of their use. If the rate at that location exceeds the rate charged by the service provider, the additional use tax must still be remitted.

OHIO - SALES AND USE TAX SOURCING RULES

Defender Security Company v. Testa

- **Receipts from Services:** As you recall, under O.R.C. § 5751.033(I), gross receipts from services and all other gross receipts are sourced based on the proportion that the purchaser's benefit in the state with respect to what was purchased bears to the purchaser's benefit everywhere with respect to what was purchased.
- The physical location where the purchaser ultimately uses or receives the benefit of what was purchased shall be paramount in determining the proportion of the benefit in the state.

Facts

- An authorized dealer for ADT Security Services, sold and installed security equipment and obtained contracts for security monitoring services, which it sold to ADT for a fee.
- Defender filed refund claims arguing that ADT, as the purchaser of the contracts, receives the benefit of Ohio-based contracts at its principal place of business outside Ohio.

OHIO - SALES AND USE TAX SOURCING RULES

Defender Security Company v. Testa

- The BTA upheld the Final Determination by the Ohio Department of Taxation (the “Department”) that the receipts from Ohio-based contracts are situated to Ohio, holding that “[t]he contracts would not exist without property in Ohio to be monitored and equipment located within such property in Ohio by which the monitoring is performed.”
- The BTA also noted that several examples in the regulations supported its conclusion, including examples involving receipts from appraisal services, architecture services, and engineering services, all of which are sourced to Ohio if the property tied to such services is located wholly in Ohio.
- The Ohio Court of Appeals affirmed this decision and Defender Security appealed the decision to the Ohio Supreme Court.

OHIO - SALES AND USE TAX SOURCING RULES

Defender Security Company v. Testa

- On September 29, 2020, the **Ohio Supreme Court reversed** the Court of Appeals, holding that Defender's receipts from selling security contracts to ADT should have been sourced to ADT's principal place of business, which was outside Ohio.
- Importantly, the Court rejected the Commissioner's argument that Defender must, in essence, look through ADT's location and source the receipts to the location where ADT's residential customers received the benefit of the security contracts.
- Thus, the Court drew a clear distinction between the services that Defender provided to ADT (situated to ADT's location) and the security monitoring services provided by ADT (situated to the location of ADT's residential customer).

OHIO

EXEMPTION CERTIFICATES

Ohio - Exemption Certificates

- All sales are presumed taxable unless a properly completed exemption certificate is received. The certificate relieves the seller of liability so long as the consumer provides the vendor or seller with all data elements required for a valid exemption certificate, the vendor may accept the certificate and be relieved of the obligation to collect the tax. Note also that exemption certificates may be presented in either paper or electronic form. Paper certificates require, as one of the data elements, a signature from the consumer. No signature is required on electronic certificates.
- **STEC-U Unit Exemption Certificate.** This exemption certificate is used to claim exemption or exception on a single purchase.
- **STEC-B Blanket Exemption Certificate.** This certificate is used to make a continuing claim of exemption or exception on purchases from the same vendor or seller.

Ohio - Exemption Certificates

- **Multistate Tax Commission Uniform Sales and Use Tax Certificate.** Ohio accepts the Uniform Sales and Use Tax Certificate created by the Multistate Tax Commission as a valid exemption certificate. By its terms, this certificate may be used only for claiming an exemption based on resale or on the incorporation of the item purchased into a product for sale. This form may be obtained on the Multistate Tax Commission's website: www.mtc.gov. The instructions on the form indicate the limitations Ohio, and other states that accept this certificate, place on its use.
- **Streamlined Sales Tax System Certificate of Exemption.** Ohio accepts the Exemption Certificate adopted by the Streamlined Sales Tax System. It may also be used to notify vendors or sellers of direct payment authority, of a claim of multiple points of use or, pursuant to section 5739.033(D) of the Ohio Revised Code, of a direct mail claim by a purchaser of direct mail. This form may be obtained on the website of the Streamlined Sales Tax Project: www.streamlinedsalestax.org

OHIO

TOOLS, MACHINERY,
AND CONSUMABLES

Ohio - Tools, Machinery, and Consumables

- **Items Used or Consumed**
- Items used or consumed by a contractor are taxable per Ohio Administrative Code 5703-9-14(H). i.e. consumable supplies.
- Items used or consumed are always taxable to the contractor. Even on exempt jobs

Tools	Dyed Diesel Fuel	Generators
Heavy Equipment	Sand Paper	Welding Gases
Rentals	Cleaning Supplies	Propane
Job Trailers	Masking Tape	Temporary Items
Portable Toiles	Tarps	Private Security
Air Compressors	Hard Hats	Temporary Employment
Scaffolding	Safety Glasses	Landscaping and Snow Removal

OHIO TAXABLE SERVICES

Ohio - Taxable Services

- In Ohio services are not subject to tax unless specifically enumerated as taxable. While not all services in Ohio are taxable, there is a list of taxable services which will be covered in the upcoming slides
- As you will see when we go over the list of taxable services, professional, personal, and insurance transactions are not taxable so long as any tangible personal property transferred is a small item for which no separate charge is made.
- For Example:
 - Company A is performing a design and build service for a customer. As part of this project it drafts blueprints for the project. Since the printing of large blueprints takes a special printer you send out the prints to a printer to print large size blueprints. When you bill your customer for the blueprint services it depends on how you bill your customer as to whether or not the any portion of the charge is taxable.
 - If you charge your customer a single lump sum charge for the blueprint services and do not break out the blueprint printing services, the entire transaction is exempt because the blueprints are an inconsequential cost of the work.
 - However, if you separately state the design services and the blueprint printing service the blueprint printing services are taxable.

Ohio - Taxable Services

- Automatic data-processing, computer and electronic-information services provided for use in business.
- Building maintenance and janitorial services (if annual sales equal or exceed \$5,000).
- Landscaping and lawn-care service (if annual sales equal or exceed \$5,000).
- ~~Provision of employment placement service. **(Repealed 10/1/2021)**~~
- ~~Provision of employment service. **(Repealed 10/1/2021)**~~
- Provision of exterminating service.
- Provision of information service (1-900 telephone calls).
- Provision of private investigation or security service.
- Satellite-broadcasting service, both audio and video.
- Snow-removal service provided by any **mechanized means**, excluding provision of such service by a person that has less than \$5,000 in sales of such service in a calendar year.
- Taxable telecommunication services.
- Cleaning towels, linen or clothing used in a trade or business.
- Installation of tangible personal property (except installation of property exempt from sales tax).

Ohio - Taxable Services

- Laundry and dry-cleaning service, excluding sales made through self-service facilities.
- Personal-care service, including skin care, application of cosmetics, manicures, pedicures, hair removal, tattoos, body piercing, tanning, massage and other similar services. It does not include the cutting,
- coloring or styling of an individual's hair, or service provided by or on the order of a licensed physician or licensed chiropractor.
- Provision of physical-fitness facility service.
- Provision of recreation and sport-club service.
- Rental of hotel rooms or similar sleeping accommodations for less than 30 consecutive days by establishments with five or more sleeping rooms.
- Repair of tangible personal property (except repair of property that is exempt from sales tax).
- Storage service for tangible personal property, except such property that the consumer of the storage holds for sale in the regular course of business. (Inventory Storage Not Taxable)
- Towing service for motor vehicles.
- Transportation of persons by motor vehicle or aircraft within Ohio, except by public transit systems, ambulance or commercial airlines.
- Washing (except coin-operated), cleaning, waxing, polishing or painting of motor vehicles.

Ohio - Taxable Services

Rentals

- The Ohio sales and use taxes apply to the retail sale, lease, and rental of tangible personal property, and there are also a number of select services that are taxable.
- As a general rule, all rentals of tangible personal property such as portable toilets, equipment, vehicles, machinery, generators, portable lighting towers, lifts, cranes, and other equipment are subject to sales tax.
- However, there when the rental includes an operator it is not considered the rental of property but the procurement of a non-taxable personal service.
 - For Example:
 - Rent a very large 20 tone crane – Since large cranes generally require an operator knowledgeable about the operation of the crane the rental generally includes an operator.
 - In this example the crane rental would be exempt from Ohio sales tax

Ohio - Taxable Services

Freight/Delivery - Charges

- Most charges to ship taxable goods are taxable in Ohio.
- Delivery charges are considered part of the sale price whether separately stated or included in the price, so they're taxable if the sale is taxable and exempt if the sale is exempt.
- If one delivery charge includes both taxable and exempt sales, it can be allocated (by weight or sale price) so tax is only charged to ship the portion of the shipment that's taxable.
- If it isn't allocated, tax applies to the whole shipping charge.
- Delivery charges not connected with a taxable sale are exempt.

OHIO

INDUSTRY SPECIFIC RULES

Ohio –Public Utilities

- Public Utility - Property or service directly used in the rendition of a public utility service eligible for exemption. The term "used directly in the rendition of a public utility service" means property that is to be incorporated into, and will become a part of, the consumer's production, transmission, transportation, or distribution system and that retains its classification as tangible personal property after such incorporation.

Ohio - Energy Projects

- **Ohio** - R.C. 5739.02(B)(40) provides an exemption for “[s]ales of tangible personal property and services to a provider of electricity used or consumed directly and primarily in generating, transmitting, or distributing electricity for use by others, including property that is or is to be incorporated into and will become a part of the consumer's production, transmission, or distribution system and that retains its classification as tangible personal property after incorporation.” There is no application process to claim the exemption. A taxpayer claiming the exemption would provide its vendor with a fully completed exemption certificate such as the STEC B, Sales and Use Tax Blanket Exemption Certificate.

Substations Overview

- Generally, electric utilities recognize three stages in providing electricity to customers:
 - **Production** - Refers to the generation of electricity, including substations. Step-up substations raise the voltage from generators to it can be transmitted efficiently
 - **Transmission** - The transfer of electricity from generating sources to local distribution systems. Step-down substations lower the voltage from the transmission lines to a subtransmission voltage, often used for industrial processing.
 - **Distribution** - The transfer of electricity from local distribution systems to the customer. Distribution substation further lowers the subtransmission voltage to one that can be used to support most industrial, commercial, and residential needs. (i.e., overhead poles and on or underground pad mount transformers)

Substations Work Taxability - OH

Worked Performed	T/NT	Clarifying Notes and Comments
Electrical Duct Bank - (Conduit, Grounding, Cable Trench)		
-Earthwork	NT	Non-taxable service
-Piping Installation - Transmission Lines	NT	Generation, transmission, and distribution exemption
Fuel Pipe Trenching (Natural Gas Fuel)	NT	Follow real property taxability. Labor exempt, purchase of materials taxable
Pier Foundations and Transmission Line Piers (Concreate, Rebar, and Anchor Bolts)	NT	Generation, transmission, and distribution exemption
Remediation (Topsoil, Seeding, Landscaping, etc.)	Mixed	Excavation work exempt / true landscaping taxable
Removal of Old Foundations	NT	Non-taxable service
Road Paving - Permanent Road (Concrete or Aggregate)	NT	Follow real property taxability. Labor exempt, purchase of materials taxable
Site Drainage	NT	Follow real property taxability. Labor exempt, purchase of materials taxable
Site Hardening Project - (Security Fencing and Associated Poles and Foundations)	NT	Follow real property taxability. Labor exempt, purchase of materials taxable
Sitework - Earthwork and Grading - (General Ground Work)	NT	Non-taxable service

Substations Work Taxability - OH

Worked Performed	T /NT	Clarifying Notes and Comments
Stoning the Yard (Spread Aggregate for Clear Work / Maintained Area)	NT	Follow real property taxability. Labor exempt, purchase of materials taxable
Storm Sewer & Drainage (Rainwater Runoff Only/No Pollution Water)	NT	Follow real property taxability. Labor exempt, purchase of materials taxable
Substation Foundations	NT	Generation, transmission, and distribution exemption
Switch Station Foundations	NT	Generation, transmission, and distribution exemption
Transmission Line Access Road	NT	Generation, transmission, and distribution exemption
Transmission Line Access Road Clearing	NT	Generation, transmission, and distribution exemption
Transmission Pole Foundations	NT	Generation, transmission, and distribution exemption

OHIO RELEVANT COURT CASES

Ohio - Relevant Court Cases

Case Law

- **Karvo Paving Co. v. Testa - Court of Appeals – Ninth District - 2019-Ohio-3974 (ODT dismissed its appeal at Supreme Court)**
- **Resale**
 - Application of the resale exemption in construction contractor context
 - Karvo audited for Ohio Consumer's Use Tax
 - Performed contracts with Ohio Department of Transportation
 - Utilized leased traffic control equipment
 - Karvo argued equipment leased for resale to ODOT
 - Previously, any and all equipment used by the contractor in performance of contract was considered used/consumed by the taxpayer

Ohio - Relevant Court Cases

Case Law

- **Karvo Paving Co. v. Testa - Court of Appeals – Ninth District - 2019-Ohio-3974 (ODT dismissed its appeal at Supreme Court)**
 - Court considered the following:
 - ODOT responsible for traffic maintenance and placed the equipment
 - Equipment continually used during off hours
 - If given a choice, Karvo would have used different equipment in a different manner
 - Court found in favor of Karvo and upheld resale exemption

Case Law

- **Karvo Paving Co. v. Testa - Court of Appeals – Ninth District - 2019-Ohio-3974 (ODT dismissed its appeal at Supreme Court)**
 - Practical application of case
 - What really qualifies? ODT will construe narrowly to equipment mentioned in case
 - Taxpayers may argue broader interpretation of equipment that qualifies
 - Applicability to temporary lane markings
 - Contracts with other political subdivisions (counties, townships, etc)
 - Impact of separate line items in bid submitted to ODOT or other political subdivision
 - What if paving and related traffic control equipment is sub-contracted?

Case Law

- **Karvo Paving Co. v. Testa - Court of Appeals – Ninth District - 2019-Ohio-3974 (ODT dismissed its appeal at Supreme Court)**
 - Examined exemption for casual sale (or lease) of equipment between affiliated entities
 - Affiliate purchased paving equipment for its own use, then stopped doing paving contracts
 - Karvo leased the equipment from affiliate
 - Court agreed that affiliate's leases to Karvo did not prevent use of casual sales exemption
 - Case remanded to BTA to analyze applicability of the casual sale exemption

Case Law

- **Karvo Paving Co. v. Testa - Court of Appeals – Ninth District - 2019-Ohio-3974 (ODT dismissed its appeal at Supreme Court)**
 - A portion of the case was remanded to BTA to analyze applicability of the casual sale exemption.
 - Decided on November 3, 2021 (Karvo Paving Co. v. McClain, BTA No. 2016-782)
 - The BTA determined that the exemption is not available since the leases systematically reoccurred and became part of the lessor’s business, rather than occasional, casual or isolated.

Ohio - Relevant Court Cases

***N.A.T. Transportation, Inc. v. McClain*, Supreme Court of Ohio, 2021-Ohio-1374 (Case No. 2020-0110)**

Case Decision Summary

- The Supreme Court of Ohio (court) ruled that a waste hauler can claim the "highway transportation for hire" sales and use tax exemption for the purchase of two trucks used to transport waste to disposal sites designated by the customer.
- The court concluded that waste remains the customer's personal property when the customer specifies where to dispose of the waste, thereby qualifying the trucks as "highway transportation for hire."
- *The issue is that the "highway transportation for hire" requires that the property be owned by another.*

Facts

- The waste hauler, was certified by the Ohio Public Utilities Commission as a for-hire motor carrier.
- The waste hauler serves residential customers through contracts with local governments or through direct subscriptions with residential customers.
- The residential customers cannot specify where the waste is disposed.
- However, the waste hauler also serves commercial, industrial and institutional customers, such as schools. Those customers designate the destination for the disposal of their waste.

Ohio - Relevant Court Cases

***N.A.T. Transportation, Inc. v. McClain*, Supreme Court of Ohio, 2021-Ohio-1374 (Case No. 2020-0110)**

- At issue was the sales tax treatment of three trucks purchased by the waste hauler.
- Two trucks were used to pick up and haul the commercial, industrial and institutional waste.
- The third truck was used to dispose residential waste.
- The Department assessed sales and use tax on the purchase of all three the trucks.
- The waste hauler argued that it was entitled to a tax exemption on the purchases of the trucks because it was certified as a for-hire motor carrier.
- The Department denied the exemption, citing the court's 2002 decision in *Rumpke Container Serv., Inc. v. Zaino*, 94 Ohio St. 3d 304, 762 N.E.2d 995 (2002) (*Rumpke*). The taxpayer appealed to the Ohio Board of Tax Appeals (BTA), which affirmed the assessment.

Ohio - Relevant Court Cases

***N.A.T. Transportation, Inc. v. McClain*, Supreme Court of Ohio, 2021-Ohio-1374 (Case No. 2020-0110)**

- Ohio Rev. Code 5739.02(B)(32) exempts from sales/use tax the sale, lease, repair, maintenance or parts of motor vehicles that are primarily used by persons engaged in highway transportation for hire to transport another's tangible personal property.
- Ohio Rev. Code 5739.01(Z) defines "highway transportation for hire" as the transportation of another's personal property, for consideration, by someone certified to transport that property on highways, roadways, streets or any similar public thoroughfare.
- As some history, in 2002, the court denied this exemption to a taxpayer in Rumpke, which addressed whether a residential waste hauler could claim the exemption.
- The BTA had denied the exemption on the grounds the taxpayer did not possess the required statutory certification.
- On appeal, the court affirmed the BTA's decision but also concluded that the taxpayer did not transport tangible personal property belonging to others because the customers relinquished control over their waste upon pickup by the taxpayer.

Ohio - Relevant Court Cases

***N.A.T. Transportation, Inc. v. McClain*, Supreme Court of Ohio, 2021-Ohio-1374 (Case No. 2020-0110)**

- In this case, the court held that the waste hauler could claim the exemption for the two trucks used to haul commercial, industrial and institutional customers' waste to landfills.
- The court based its ruling on the finding that the waste remained the personal property of the customer because the customer told the taxpayer where to dispose of the waste.
- In so holding, the court distinguished the facts in this case from those in Rumpke, finding that that the waste hauler in Rumpke not only owned the trucks and hauled the waste but also owned the landfills to which it was taken and, as such, was not transporting personal property belonging to others.
- The court determined that the owner could not claim the exemption for the truck used to transport waste for residential customers because those customers did not designate where to dispose of the waste.

Ohio - Relevant Court Cases

***N.A.T. Transportation, Inc. v. McClain*, Supreme Court of Ohio, 2021-Ohio-1374 (Case No. 2020-0110)**

Potential Implications

- Taxpayers engaged in hauling waste should consider both *Rumpke* and this new decision in *N.A.T. Transp. Inc.* in considering whether their operations could qualify for the sales and use tax exemption.
- For some similarly situated waste haulers, refunds of sales tax may be available. The statute of limitations for refunds is four years from the payment of the tax.

Ohio - Relevant Court Cases

Opinion of Tax Commissioner (Opinion 20-0001), Port Authority Construction Contracts

Facts

- The Port Authority intends to ground lease from Taxpayer certain real property
- In the project site, the Port Authority intends to construct a XXXXXX.
- The XXXX project site, the Port Authority intends to construct a XXXXX.
- The Port Authority intends to construct the projects through a construction management agreement with Taxpayer or one or more of Taxpayer's affiliates.
- Taxpayer is entirely responsible for the construction of the projects pursuant to the construction management agreement. The projects will be incorporated in to underlying real property

Ohio - Relevant Court Cases

Opinion of Tax Commissioner (Opinion 20-0001), Port Authority Construction Contracts

Facts

- At the same time the ground lease is executed, the Port Authority will lease the projects and the project sites to Taxpayer.
- The Port Authority has no obligation to fund any portion of the projects other than a portion financed through the issuance of taxable lease revenue bonds.
- The bonds will be purchased by Taxpayer or one or more of Taxpayer's affiliates and are payable solely from rental payments made by Taxpayer under the lease. Other than those lease payments, no other funds from the Port Authority are available to pay debt service on the bonds.
- The Port Authority will continue to own the projects subject to the leasehold rights of Taxpayer, and Taxpayer will have the option to terminate the lease and the ground lease and acquire the projects at any time after the fifth anniversary of the lease. Taxpayer intends to use the projects and the project sites XXXXXXXXXXXXXXXXXX for its business.

Ohio - Relevant Court Cases

Opinion of Tax Commissioner (Opinion 20-0001), Port Authority Construction Contracts

- **Requested Opinion**

1.) Whether building and construction materials sold to construction contractors for incorporation into real property that will be owned by the Port Authority and leased to Taxpayer are exempt from Ohio sales and use tax pursuant to R.C.5739.02(B)(13)

Ohio - Relevant Court Cases

Opinion of Tax Commissioner (Opinion 20-0001), Port Authority Construction Contracts

- **Requested Opinion**

- Whether building and construction materials sold to construction contractors for incorporation into real property that will be owned by the Port Authority and leased to Taxpayer are exempt from Ohio sales and use tax pursuant to R.C.5739.02(B)(13).

- **APPLICABLE LAW**

- Generally, a construction contract pursuant to which tangible personal property is incorporated into and becomes a part of real property is not a “sale”, and a construction contractor is the consumer of the incorporated tangible personal property and liable for the tax.

Ohio - Relevant Court Cases

Opinion of Tax Commissioner (Opinion 20-0001), Port Authority Construction Contracts

- However, the tax does not apply to:
 - Building and construction materials and services sold to construction contractors for incorporation into a structure or improvement to real property under a construction contract with this state or a political subdivision of this state, or with the United States government or any of its agencies; or
 - Building and construction materials and services sold to construction contractors for incorporation into a structure or improvement to real property that are accepted for ownership by this state or any of its political subdivisions, or by the United States government or any of its agencies at the time of completion of the Structures or improvements

Ohio - Relevant Court Cases

Opinion of Tax Commissioner (Opinion 20-0001), Port Authority Construction Contracts

OPINION OF THE TAX COMMISSIONER

- Building and construction materials sold to Taxpayer which are incorporated into real property subject to the construction contract with the Port Authority qualify for exemption pursuant to R.C.5739.02(B)(13).
- Machinery, equipment, tools, supplies and other tangible personal property used or consumed in performing a construction contract, including a contract with an Ohio political subdivision, and that are purchased or leased by Taxpayer are taxable.
- Tangible personal property which is temporarily affixed during construction including items that remain affixed after completion of construction due to inadvertence, convenience or economic necessity are not “incorporated into real property” and therefore do not qualify for the exemption in R.C.5739.02(B)(13).

MICHIGAN

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Summary of experience

Ralph Ourlian provides state and local tax services specializing in a number of industries: Industrials (manufacturing), Consumer Products (retail) and Business Professional Services. Ralph has practiced in public accounting for 25 years, most of that being in the Big 4. He specializes in income & franchise taxes, both compliance and consulting; and state controversy projects. Ralph has led several VDA, nexus studies and state audit defense projects. Ralph also works in other state and local tax services: property taxes and sales and use taxes. In addition, Ralph has worked on many ASC 740 projects focused on the state side.

Over the years, Ralph has delivered significant value to his clients and supervised large outsource tax compliance projects. Ralph has served as the state desk in Michigan reviewing and signing off on complex state and local tax transactions, positions and refund claims. In addition, Ralph is a contributor and speaker at the annual Michigan Tax Conference.

Professional affiliations and credentials

- Certified public accountant, Michigan
- American Institute of Certified Public Accountants
- Michigan Association of Certified Public Accountants

Education

- Bachelor of Science, accounting, Wayne State University

MICHIGAN CONSTRUCTION CONTRACTORS

MICHIGAN

REAL PROPERTY VS.
TANGIBLE PERSONAL
PROPERTY

Michigan – Real Property vs. Tangible Personal Property

- **Real property** is defined in Black’s Law Dictionary (8th ed) as “land, and anything growing on, attached to, or erected on it, excluding anything that may be severed without injury to the land.” Realty and real estate have the same meaning as real property.
- **Fixture** implies something having a possible existence apart from the realty which by annexation may be assimilated into realty.
- **Tangible Personal Property or Fixture to Real Estate**
- Property can lose its character as tangible personal property by transformation into a fixture when **affixed** to real estate. The relevant facts should be viewed on a case-by case basis to determine whether personal property has become sufficiently affixed to real property that it should be treated as part of the real property.

Michigan – Real Property vs. Tangible Personal Property

Examples:

- Agricultural exemption generally excludes tangible personal property permanently affixed and becoming a structural part of real estate
- Industrial processing exemption does not apply to tangible personal property affixed and becoming a structural part of real estate in Michigan
- A taxpayer selling tangible personal property is required to pay sales tax on retail sales
- A contractor with tangible personal property that is permanently affixed to and considered to be part of realty has a use tax liability as a consumer of the property

Michigan—Real Property vs. Tangible Personal Property

Three Factors to Consider

- **1.) Annexation to realty, either actual or constructive**
 - This factor has to do with the manner in which an item is attached to the real property. There are many ways that a person can affix personal property to real estate; some items may be physically attached to the real estate (e.g., bolted to the floor or wall) whereas other items may be put in place with the intent that the property will become part of the real estate through size and character. Therefore, even if an object is not physically affixed to the realty, it may acquire the status of a fixture by constructive annexation.
- Constructive annexation has frequently been applied in the case of property which is not itself actually or directly annexed to the realty, but is part of, or accessory to, property which is annexed. The property, if removed, would leave the property to which it is annexed unfit for use and the part or accessory is not capable of general use elsewhere.

Michigan—Real Property vs. Tangible Personal Property

Three Factors to Consider

1.) Annexation to realty, either actual or constructive

- There is no universal test whereby the character of what is claimed to be a fixture can be determined. Normally whatever is affixed to a building by an owner to complement, to facilitate its use and occupation in general, becomes a part of the realty, though capable of removal without injury to the building.
- Certain equipment remains personal property even though it may appear to be part of real property. Since some items can have the appearance of being real property, it is important to ascertain all the facts before making a final decision.
- If the object is not attached to the land or to some structure or appliance which is attached to the land, it will retain its character as personal property even though intended for permanent use on the premises.
- Generally, if property depends on the building utilities for operation and use and is connected to the building utilities (e.g. gas, electric, plumbing.), it is deemed to be affixed to realty

Michigan–Real Property vs. Tangible Personal Property

Three Factors to Consider

2.) Adaptation or application to the use or purpose of the real estate

- This factor suggests that if an item functions as part of the particular building or if it carries out part of the function of the real property, that item is probably real property. An object introduced onto the realty may become a fixture if it is a necessary or at least a useful adjunct to the realty, considering the purpose to which the latter is devoted.
- **Examples:**
 - Screens which are built to fit the windows of a particular building
 - Theater seats bolted to the theater floor and an essential part of the function of the building
 - Another indicator of real property exists when the object cannot be used unless affixed to the building or land
 - Drive-up window equipment
 - Vault doors and Night depository equipment
- In summary, if the tangible personal property serves a function of realty or the building and if it is attached to realty and permanently affixed to realty, it would usually be considered real property

Michigan—Real Property vs. Tangible Personal Property

Three Factors to Consider

3.) Intention to make the property a permanent accession to the real estate

- Whether attached property becomes a fixture depends largely upon the intention of the parties. Objective visible facts of the party making the annexation determines the intent.
- The permanence required is not equated with perpetuity.
- It is sufficient if the item is intended to remain where affixed until worn out, until the purpose to which the realty is devoted is accomplished, or until the item is superseded/replaced by another item more suitable for the purpose.
- Permanency of the attachment, and its character in law, do not depend so much on the degree of physical force with which the thing is attached, or the manner and means of attachment, as upon the motives and intention of the party in attaching it.
- If the intention is that the articles attached will not by annexation then it is classified as fixture

Michigan—Real Property vs. Tangible Personal Property

Three Factors to Consider

3.) Intention to make the property a permanent accession to the real estate

- Intent may be inferred from the nature of the article affixed, the purpose for which it was affixed, and the manner of annexation. Whatever is affixed to a building by an owner to complement, to facilitate its use and occupation in general, becomes a part of realty, though capable of removal without injury to the building.

[\(See Real Property vs. Personal Property Chart\)](#)

MICHIGAN DELIVERY CHARGES AND INSTALLATION

Michigan - Delivery Charges and Installation

- Delivery charges are taxable when they fall within the statutory definitions, but they are “*not taxable*” when they do not, instead of “*exempt.*” they are “excluded” from the definition of “price” or “sale”. This is important when considering who bears the burden of proof.
- Delivery charges are charges by the seller for preparation and delivery to a location designated by the purchaser of tangible personal property or services.

Michigan - Delivery Charges and Installation

“Sales price” for Sales Tax purposes and “price” for Use Tax purposes include:

“Delivery charges incurred or to be incurred before the completion of the transfer of ownership of tangible personal property subject to the tax levied under this act from the seller to the purchaser.”

- Whether or not handling charges associated with the delivery of tangible personal property are taxable depends on when the delivery takes place.
- Michigan tax law includes “handling charges” for sales of tangible personal property or services within the meaning of “delivery charges,” and therefore such charges are treated in the same manner as delivery charges.

Michigan - Delivery Charges and Installation

- In determining whether ownership of property is transferred before or after delivery, the Department of Treasury **looks at the following factors:**
 - Whether the customer has the option to either pick up the property or have the property delivered;
 - Whether the delivery charge is separately negotiated and contracted for on a competitive basis;
 - Whether the property and delivery charges are separately invoiced;
 - Whether the taxpayer's books and records separately identify the transactions used to determine the tax on the sale at retail;
 - Whether delivery service records indicate a net profit (i.e., the delivery or installation service is a commercial endeavor separate from the retail business);
 - The time at which risk of loss transfers from seller to buyer;
 - The time at which title to the property passes from seller to buyer; and
 - Any other information that is relevant in determining when ownership transfers.

Upon audit they look at all of the above “together” to make a determination. So just become one of the above it satisfied it does not conclusively determine taxability

Michigan - Delivery Charges and Installation

- ***Delivery Charges***
- ***Includes***, but not limited to:
 - Transportation,
 - Shipping,
 - Postage,
 - Handling,
 - Crating,
 - Packing.
- ***Does not include*** charges for delivery of direct mail if the charges are separately stated on an invoice or similar billing document given to the purchaser.

Michigan - Delivery Charges and Installation

- Charges allocated between exempt and taxable property at the discretion of the seller.
 - **Two ways to allocate:**
 - (i) Delivery price x (total sales prices of taxable property / total sales prices of shipment).
 - (ii) Delivery price x (total weight of the taxable property / total weight of shipment).
 - MCL 205.51a(e) of the STA; MCL 205.92b of the UTA.
- A seller is not liable for sales tax on delivery charges allocated to the delivery of exempt property. MCL 205.51(1)(d)(iv).

Michigan - Delivery Charges and Installation

“**Installation charges** incurred or to be incurred before the completion of the transfer of ownership of tangible personal property from the seller to the purchaser.”

- MCL 205.51(1)(d)(v); MCL 205.92(f)(v).
- “Installation charges” are not defined in the STA and UTA.

MICHIGAN STATUTORY EXEMPTIONS

Michigan–Statutory Exemptions

Exemptions – Flow Through to Contractor

- The only exemption(s) for contractors purchasing materials is for materials that are affixed and made a structural part of real estate for a qualified nonprofit hospital or a nonprofit housing entity qualified as exempt under the Sales and Use Tax Acts, made a structural part of a sanctuary for a church, or is a component part of an air or water pollution facility for which a tax exemption certificate has been issued by the State Tax Commission.

How to Claim Exemption from Suppliers

- You should receive [Form 3520 from the property owner](#), Michigan Sales and Use Tax Contractor Eligibility Statement from your customer, and you will need to retain a copy.
- To purchase materials for the contract exempt from sales/use tax the contractor must provide a completed [Form 3372](#), Michigan Sales and Use Tax Certificate of Exemption and provide a copy of [Form 3520](#) that you received from your customer.
- **Both of these documents (Form 3372 and Form 352) are required and the contractor to keep in both in their files.**

Michigan–Statutory Exemptions

Common Sales and Use Tax Exemptions and Requirements

- **501(c)(3) and 501(c)(4) Organizations** – 501(c)(3) and 501(c)(4) organizations must provide proof that they are exempt under these codes by the Internal Revenue Service. In addition to this they must provide a certificate of exemption stating that the property will be used or consumed in carrying out the operations of the organization. Revenue Administrative Bulletin [1995-3](#) and [2002-15](#) has more information on this topic.
- **Wholesalers** purchasing for resale should provide the seller with a completed form [3372 Michigan Sales and Use Tax Certificate of Exemption](#) and check the box for **Resale at Wholesale**. Sales tax licenses are not issued to wholesalers.
- **Retailers** – Retailers purchasing for resale should provide a signed exemption certificate by completing form [3372 Michigan Sales and Use Tax Certificate of Exemption](#) and check box 1. For Resale at Retail in Section 3, Basis for Exemption Claim. Their sales tax license number must be included in the blank provided on the exemption claim. However, a seller should not accept the sales tax license number alone as a claim of exemption. The department does not issue tax-exempt numbers.

Michigan–Statutory Exemptions

Common Sales and Use Tax Exemptions and Requirements

- **Industrial Processors** – An industrial processing exemption is allowed for property which is used or consumed in transforming, altering, or modifying tangible personal property by changing the form, composition, or character of the property for ultimate sale at retail or for sale to another processor for further processing and ultimate sale at retail. The industrial processing exemption does not include property which is or becomes affixed to real estate, office supplies, administrative office equipment, or vehicles licensed for public highway use, except when the vehicle is used to mix and agitate materials added at the plant or job site in the concrete manufacturing process. Industrial processing also does not include the receipt or storage of raw materials extracted by the user or consumer or the preparation of food or beverages by a retailer for retail sale. The exemption certificate is [3372 Michigan Sales and Use Tax Certificate of Exemption](#) .
- **Hospitals** – Sales to hospitals are exempt from sales tax when the organization is not operated for profit. The income or benefit from the operation must not inure to any individual or private shareholder, directly or indirectly. [Revenue Administrative Bulletin 1995-3](#) and [2002-15](#) has more information on this topic.

Michigan—Statutory Exemptions

Common Sales and Use Tax Exemptions and Requirements

- **Church Sanctuary** - The building must be owned, occupied, and used by a religious organization qualified under section 501(c)(3) of the internal revenue code of 1986.
- The exemption is limited to building portions that are predominantly (50%) and regularly used for worship service.
- Total material purchases for multiple use areas (such as roofs and foundations) and where a single piece of equipment (such as a furnace) is supplying qualified sanctuary areas as well as other non-exempt areas, an apportionment formula is used to derive a taxable percentage:
 - Sanctuary Square Footage divided by the Total Building Square Footage
- **Schools** – Sales to schools and parent cooperative preschools are exempt from sales tax when the organization is not operated for profit. The income or benefit from the operation must not inure to any individual or private shareholder, directly or indirectly. PTA, PTO, and all other groups and organizations must qualify separately for exemption when making purchases for their organizations. Sales to teachers are subject to tax. [Revenue Administrative Bulletin 1995-3](#) and [2002-15](#) has more information on this topic.

Michigan–Statutory Exemptions

Common Sales and Use Tax Exemptions and Requirements

- **Government** – Sales to the United States government, the State of Michigan and its political subdivisions, departments and institutions are not subject to tax, if the sales are ordered on the government form or purchase order and are paid for directly to the seller by warrant on government funds. Sales to the American Red Cross, and its chapters and branches are exempt. All sales to other states or countries are subject to Michigan sales tax. Sales to employees of the government for their own use are subject to tax. The exemption certificate is [3372 Michigan Sales and Use Tax Certificate of Exemption](#)

Michigan–Statutory Exemptions

Michigan Sales and Use Tax Contractor Eligibility Statement (Form 3520)

- Contractors claiming an exemption when purchasing materials used in an exempt construction contract should obtain a statement from the property owner that materials to be affixed to and made a structural part of certain real property qualify for exemption based on facts within the control of the property owner.
- The property owner should complete the form and return it to the contractor who will submit this form to the supplier along with Michigan’s Sales and Use Tax Certificate of Exemption, form 3372 at the time of purchase. Nothing in this statement should be construed to relieve a contractor from tax liability if it is found that the subject property does not qualify for the exemption.
- These exemptions apply to all types of contractors that affix tangible personal property to realty. There is no exemption for supplies, electricity, natural gas and other items consumed by the contractor and not affixed to realty.

A contractor in the business of constructing, altering, repairing, or improving real estate for others is afforded an exemption for property affixed to and/or made a structural part of real estate that qualifies under one of the following: **Continued on the next several slides**

Michigan–Statutory Exemptions

Nonprofit Hospitals

- The General Sales Tax Act and Use Tax Act states that tangible personal property sold to a person directly engaged in the business of constructing, altering, repairing or improving real estate for others is exempt to the extent that the property is “affixed to and made a structural part of” a nonprofit hospital. The statute requires that a hospital comply with the following two tests to be met in order for this exemption to apply:
 - Meet the statutory definition of a “nonprofit hospital,” and
 - Pass the inurement (benefit) test.
- **Nonprofit hospital** means one of the following:
- **1.)** That portion of a building to which one of the following applies:
 - Is owned or operated by an entity exempt under Internal Revenue Code (IRC) § 501(c)(3), that is licensed as a hospital
 - Is owned or operated by a governmental unit in which medical attention is provided
 - Is owned or operated by an exempt entity or entities exempt under IRC § 501(c)(2) or (3)

Michigan–Statutory Exemptions

Nonprofit Hospitals

- **2.)** That portion of real property necessary and related to a building described in 1 above, in which medical attention is provided. “Medical attention” means “that level of medical care in which a physician provides acute care or active treatment of medical, surgical, obstetrical, psychiatric, chronic, or rehabilitative conditions, that require the observation, diagnosis, and daily treatment by a physician.
- A county long-term medical care facility (CLTMCF), including any “addition” to an existing county long-term medical care facility, if the addition is owned and operated by the CLTMCF and offers health services provided by the CLTMCF
- A CLTMCF is “a nursing care facility, other than a hospital long-term care unit, that provides organized nursing care and medical treatment to 7 or more unrelated individuals who are suffering or recovering from illness, injury, or infirmity and that is owned by a county or counties.” Operations not requiring licensure, such as “assisted living facilities,” do not qualify as a hospital for the construction exemption.

Michigan–Statutory Exemptions

Nonprofit Hospitals

- In the case of a CLTMCF, “affixed to and made a structural part of” means any physical connection to an existing CLTMCF. Therefore, the exemption for a CLTMCF is limited to tangible personal property that ultimately has any physical connection to any addition to or renovation of an **existing building of a CLTMCF**. The exemption is only available for newly constructed buildings if the building has a physical connection to an *existing* CLTMCF building (e.g., by breezeway). If no such physical connection exists, the exemption may not be claimed.
- Nonprofit hospital **does not include** the following:
 - A freestanding building (unless a qualifying addition to a county long-term medical care facility) or other real property of a nursing home or skilled nursing facility
 - A licensed hospice
 - A licensed home for the aged

Michigan–Statutory Exemptions

Nonprofit Hospitals

- ***Inurement of Benefit Test***

Any portion of property that otherwise qualifies as a nonprofit hospital must also pass the **inurement of benefit test**. That is, no income or benefit may inure directly or indirectly to an individual, private stockholder or other private person from the independent or nonessential operation of that portion of the property. This exemption may be calculated on a pro rata basis. A nonprofit hospital passing the inurement of benefit test would qualify for exemption.

- However, where a single building is being constructed that will have multiple uses, some of which will not pass the inurement of benefit test, that portion not meeting the test will be taxable.
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Michigan—Statutory Exemptions

Nonprofit Hospitals

- ***Inurement of Benefit Test***

For example, in the nonprofit hospital context, portions of the hospital building not meeting the test include, but are not limited to, these which would be rented or provided to persons to conduct commercial activities such as:

- Physicians (for private practice)
 - Pharmacy
 - Gift shop
 - Coffee shop
 - News stand
 - Medical apparatus outlet
 - Cafeteria
- **Example:** Medical Center is a nonprofit hospital. A portion of Medical Center is constructed to house a retail gift shop that will be operated by ABC Inc. Profits made by ABC inure to its private owner. The portion of Medical Center that is constructed to house the retail gift shop is not eligible for the exemption.

Michigan—Statutory Exemptions

Nonprofit Hospitals

- ***Inurement of Benefit Test***

Example: ABC, a county long-term medical care facility, hires a contractor to construct a freestanding building on ABC's existing campus. The new building will be used as an office and not operated under ABC's license or otherwise offer the same medical services as ABC. The exemption does not apply to this transaction because the freestanding building will not be operated under the same license held by ABC or continue to offer the same medical services as ABC.

- **Example:** XYZ, a county long-term medical care facility, hires a contractor to construct a freestanding building on its existing campus that will be operated under XYZ's license and will offer the same health services as XYZ. This project is eligible for the exemption provided the qualifying transactions occurred on or after January 1, 2013.

Michigan—Statutory Exemptions

Nonprofit Hospitals

- ***Inurement of Benefit Test***

Example: Contractor is hired by developer to construct a new campus of freestanding buildings with each building licensed and operated as a county long-term medical care facility. No existing county long-term medical care facility operates on the proposed campus. **This project is not eligible for the exemption because the exemption only applies to an existing county long-term medical care facility.**

- Generally, the exemption only includes property that is affixed to and made a structural part of the nonprofit hospital. The exemption does not include tools and equipment, or supplies used and consumed in the construction which do not become a structural part of the hospital, e.g., sandpaper, hammers, saws.

Michigan—Statutory Exemptions

Qualified Nonprofit Housing

- Property used in certain improvements to real estate is exempt, including property purchased by a person directly engaged in the business of constructing, altering, repairing, or improving real estate for others to the extent that the property is affixed to and made a structural part of the real estate of a nonprofit housing entity qualified as exempt pursuant to Section 15a of the, Act No. 346 of Public Acts of 1966 (**State Housing Development Authority Act, or SHDAA**).
- Qualified nonprofit housing includes only that portion of the property of the homes or dwelling places constructed by a qualified nonprofit housing entity, the income or property of which does not directly or indirectly inure to the benefit of an individual, private stockholder or other private person.
- A nonprofit housing entity must be qualified as exempt pursuant to the SHDAA. Government housing projects are generally not in compliance with SHDAA, thus tangible personal property affixed to them is taxable. If a benefit from any portion of the real estate inures directly or indirectly to an individual, private stockholder or other private person, that portion of the property would be taxed. Additionally, no direct or indirect benefit can inure to any person other than the intended qualified tenants.

Michigan–Statutory Exemptions

Qualified Nonprofit Housing

- Only private qualified nonprofit housing that has received an exemption certificate from the Michigan Housing Development Authority (MSHDA) qualifies for this exemption. Public nonprofit housing is not covered by MSHDA and therefore does not qualify for exemption.

Michigan—Statutory Exemptions

Church Sanctuaries

- The General Sales Tax Act and Use Tax Act state that tangible personal property purchased or acquired by a contractor to be affixed to or made a structural part of a **sanctuary** of a regularly organized church or house of religious worship is exempt from sales and use tax. Therefore, the exemption does not include tools and equipment, or supplies used and consumed in the construction which do not become a structural part of the sanctuary, e.g., sandpaper, hammers, saws. The sanctuary must be owned, occupied and used by a religious organization qualified under IRC § 501(c)(3). Sanctuary includes a sanctuary to be constructed that will be owned, occupied, and used by a religious organization qualified under IRC § 501(c)(3). The exemption is limited to building portions predominately and regularly used for public worship service.

Michigan–Statutory Exemptions

Church Sanctuaries

- **Predominant use** means that public worship occurs more than 50% of the time that the building portion is in use (includes storage). **Regular use** means normal or usual periodic use or uniform use of that portion of the building. As used in this section, a sanctuary is limited to:
 - 1.) Portions of a building where the acts of worship take place, including areas where the public participates in worship, areas dedicated to individual worship (such as chapels), and those portions of the building whose sole use and function is directly related to the act of public worship.
 - These areas may also include:
 - Sacristy or similar area adjacent to room where public worship services are conducted
 - Areas where consumables are prepared for use in worship service
 - Vestry or similar area adjacent to room where public worship is conducted or where clergy or other religious leaders prepare for public worship service

Michigan–Statutory Exemptions

Church Sanctuaries

- Does not include areas for:
 - Social functions
 - Schooling
 - Day care
 - Religious Education
 - Or any other activity that does not constitute public worship
- 2.) Portions of a building structurally necessary (directly connected) to the portion of the building where worship takes place.
- These areas may include:
 - Foundations, including basement walls which support the interior worship area
 - Exterior walls and finishing materials directly adjacent to worship area
 - Interior walls, floors and ceilings facing the interior ceiling area
 - Roofs directly over the interior worship area

Michigan–Statutory Exemptions

Church Sanctuaries

- These areas would **not** include:
 - That portion of exterior walls, foundations and roofs that extend beyond the interior worship area
 - These areas may be apportioned:
 - Roofs not directly over interior worship area (i.e., roof over second story office above interior worship area)
 - Structural necessities supplying heat, ventilation and air conditioning to qualified sanctuary and non-exempt areas
 - Material purchases for multiple use areas in lieu of accounting for actual cubic yards of concrete or squares of roof shingles directly under or over the sanctuary
- In general, building areas not provided exemption include gymnasiums, offices, vestibules, hallways, restrooms, basements and classrooms. Outdoor areas such as parking lots, sidewalks and steps leading into a building are not exempt
Basement floors and second story flooring are not exempt.

Michigan–Statutory Exemptions

Qualified Water or Air Pollution Control Facilities

The General Sales and Use Tax Acts allow an exemption for the sale or purchase of tangible personal property to be installed as a component part of a water or air pollution control facility.

- “Facility” means any disposal system, including disposal wells or any treatment works, appliance, equipment, machinery, or installation constructed, used, or placed in operation primarily for the purpose of reducing, controlling, or eliminating water pollution caused by industrial waste. The following are types of facilities that would normally qualify for real and personal property, sales and use tax exemption status under PA 451 of 1994, Part 37, as amended providing they are found to be functioning adequately:
 - Industrial wastewater treatment or pretreatment installations and ancillary equipment such as wastewater storage and chemical treatment storage tanks, pumps, piping, electrical, instrumentation and sludge dewatering equipment

Michigan–Statutory Exemptions

Qualified Water or Air Pollution Control Facilities

- **b.** Waste disposal wells and monitoring wells
- **c.** Purge wells and treatment systems for industrially contaminated groundwater
- **d.** Incinerators or other technologies that effectively destroy hazardous industrial wastes that are potential water contaminants
- **e.** Landfill components that serve primarily for the purpose of reducing water pollution such as Leachate Collection Systems
- **f.** Containment dikes, impervious flooring or other containment structures to retain spillage or leakage from chemical storage tanks or hazardous waste containers
- **g.** Industrial cooling water regeneration systems and wastewater recycle systems. Pumps and piping to the system would qualify, but not return pumps and piping back to the process
- **h.** Laboratories and lab equipment used in connection with industrial wastewater pollution control

Michigan–Statutory Exemptions

Qualified Water or Air Pollution Control Facilities

- **i.** Agricultural facilities that have a primary purpose of water pollution control, such as animal waste storage facilities, pesticide and fertilizer storage facilities and certain land use changes such as green belts and filter strips that are installed and maintained to prevent water pollution
- **j.** Well casings and other measures that prevent losses to drinking water aquifers from production wells

The exemption is dependent **on a tax exemption certificate issued by the State Tax Commission (STC)**. Issuance of a certificate is contingent upon satisfying the conditions found in the Natural Resources and Environmental Protection Act

The pollution control exemptions in the Sales and Use Tax Acts are interpreted as follows:

- **1.** Tangible personal property purchased for installation as a component part of an air or water pollution control facility for which the STC issues a tax exemption certificate is exempt from tax. The certificate describes the property that qualifies for tax exemption. It includes items that become part of real property. **The flow-through exemption applies when the contractor purchases exempt personal property for these pollution control projects**

Michigan–Statutory Exemptions

Qualified Water or Air Pollution Control Facilities

- **2.)** When tax has been paid on tangible personal property which later qualifies for exemption as a result of obtaining a certificate of exemption from the STC, a refund may be requested by the purchaser upon submission of both of the following documents to the Department:
 - A copy of the exemption certificate issued, indicating the approved cost of the tangible personal property installed and entitled to exemption
 - A copy of the seller’s invoice showing the name and address of the seller, identification of the purchaser, identification of the items purchased, date of purchase and amount of tax paid to the seller
- To facilitate the refund process, the owner of the pollution control facility can provide the Department’s Tax Processing Division with a copy of the Pollution Control Exemption Certificate, together with a list of vendor invoices qualifying for the sales tax credit. That division will respond with approval or disapproval to facilitate the refund process;

Michigan–Statutory Exemptions

Pollution Control Exemption Certificates and Limitations

- An entity must apply for and be granted a pollution control exemption certificate by the STC in order for any of its purchases to qualify for this exemption. The effective date of the certificate is the date of issue and the certificate continues in force until it is revoked, or the facility is no longer used for its primary purpose. The certificate will state the total cost of the property entitled to exemption. If the final cost of material in the pollution control facility exceeds this amount, amounts exceeding the limitation are subject to tax. Furthermore, replacement equipment and repair parts acquired in subsequent years may be taxable items if the additional costs would cause the project to exceed the stated exempt value in the original exemption certificate

Michigan–Statutory Exemptions

Pollution Control Exemption Certificates and Limitations

- After review by the Property Services Division, a recommendation is made to the STC regarding the qualifications of the application. The STC is responsible for final approval and issuance of certificates. **Exemptions are not effective until approved by the STC.** However, even if a certificate is granted for the pollution control facility, the pollution control facility exemption is limited in scope to property purchased/sold and installed as a component part of such a facility. **Thus, not all property which may be associated with the construction, installation, etc. of a pollution control facility qualifies for the exemption.** Equipment benefiting the business or personnel will be taxable. Examples include, but are not limited to, heat recovery equipment, air make-up units, equipment used to prepare and return contaminants to the process, etc. **The utility costs associated with the operation of these facilities also do not qualify for the exemption.**
- A list of Pollution Control Exemption Certificate:
 - [Form 3828 – Application for Air Pollution Control Tax Exemption Certificate](#)
 - [Form 891 - Application for Water Pollution Control Tax Exemption Certificate](#)

Michigan–Statutory Exemptions

Transformational Brownfields

- Brownfields are contaminated, blighted, functionally obsolete or historic properties

- The sale of tangible personal property for use in (or acquired by a contractor for) eligible activities described in section 2 of the Brownfield Redevelopment Financing Act on **eligible property** that is included in a **transformational brownfield plan**, **to the extent that the tangible personal property will be affixed to and/or made a structural part of the real property or **infrastructure improvements** included within the transformational brownfield plan.**
- “Eligible property”, “infrastructure improvements”, and “transformational brownfield plan” mean those terms as defined in section 2 of the Brownfield Redevelopment Financing Act.
- The tangible personal property to be affixed to “and” made a structural part of the “real property or infrastructure improvements” included within the transformational brownfield plan the real estate. 2017 PA 49 requires the tangible personal property to be affixed to “or” made a structural part of the “improvements to real property” included within a transformational brownfield plan”

Michigan–Statutory Exemptions

- ***Qualified Data Centers***

Beginning January 1, 2016, through December 31, 2035, data center equipment that is affixed to or made a structural part of a qualified data center is exempt from the sales and use tax.

- For purposes of this exemption, “data center equipment” means only computers, servers, routers, switches, peripheral computer devices, racks, shelving, cabling, wiring, storage batteries, back-up generators, uninterruptible power supply units, environmental control equipment, other redundant power supply equipment, and prewritten computer software used in operating, managing, or maintaining the qualified data center or the business of the qualified data center or a co-located business. Data center equipment also includes any construction materials used or assembled under the qualified data center's proprietary method for the construction or modification of a qualified data center, including, but not limited to building materials, infrastructure, machinery, wiring, cabling, devices, tools, and equipment that would otherwise be considered a fixture or related equipment. Data center equipment does not include any equipment owned by a third party that is used to supply the qualified data center’s primary power.

Michigan–Statutory Exemptions

Qualified Data Centers

“Qualified data center” means:

- **a.)** facility composed of 1 or more buildings located in this state
- **b.)** which is owned or operated by an entity engaged at that facility in operating, managing, or maintaining a group of networked computers or networked facilities for the purpose of centralizing, or allowing 1 or more co-located businesses to centralize, the storage, processing, management, or dissemination of data of 1 or more other persons who is not an affiliate of the owner or operator of a qualified data center or of a co-located business
- **c.)** the entity that owns or operates the facility receives 75% or more of its revenue from co-located businesses that are not an affiliate of the owner or operator of the qualified data center

Michigan–Statutory Exemptions

State/Tribal Tax Agreements

- Certain tax exemptions may apply to contractors that enter into contracts involving federally recognized Indian Tribes (and their qualifying members) that have an effective tax agreement with the State of Michigan.
- Materials that are purchased, used or acquired in the performance of a contract entered into by a Resident Tribal Member, Tribe, or Tribal Entity for construction, renovation or improvement of real property owned by the Tribe or the federal government in trust for the Tribe are exempt from both sales and use taxes if the real property is located within the Tribal and Trust Lands and there is no contractual entitlement for a non-Resident Tribal Member or non-Tribal Entity to remove the improvement
- Materials that are purchased, used or acquired in the performance of a contract for construction, renovation or improvement to the principal residence of a Resident Tribal Member are exempt from both the sales tax and use tax.

Michigan–Statutory Exemptions

State/Tribal Tax Agreements

- Where the Tribe requesting exemption has opted for the certificate method, the contractor must secure a Tribal Certificate of Exemption (TCE), and a copy of the Letter of Authorization issued by the Department to the Tribe. The contractor presents this information to the vendor to purchase materials tax-free. Where the contractor is a subcontractor not identified on the TCE, a Michigan Sales and Use Tax Exemption Certificate (Form 3372) must be completed by the sub-contractor and provided to the vendor in addition to the TCE and Letter of Authorization.
- Tribes with State/Tribal Tax Agreements are listed on the Michigan Treasury Website. These agreements dictate the terms of the exemptions for the Tribes and their qualifying members for those taxes covered under the Tax Agreement(s). State law applies to those taxes where not otherwise altered by the Tax Agreement(s)

Michigan–Statutory Exemptions

State/Tribal Tax Agreements

- **Note:** Contractors engaged in the construction of Tribally-owned facilities may qualify for an exemption if **all of the following criteria are met:**
 - The facility is constructed either on Tribal and Trust Lands with regard to commercial properties (e.g., casino) or within the “government specified areas” for Tribal governmental functions as described in § III(A)(1)(b) of the Tax Agreement(s)
 - The Tribe has an effective tax agreement with the State
 - The construction contract does not entitle anyone other than the owner (e.g., Tribe, Resident Tribal Member or Tribal Entity) to remove the facility or improvement
 - The documentation identified above is completed and used appropriately
 - [There is a listing of the State/Tribal Agreement and Amendments](#)

Michigan–Statutory Exemptions

Foundations for Certain Machinery or Equipment Used in Industrial Processing

- The Acts exempt “foundations for machinery or equipment...used in an industrial processing activity...” “Industrial processing” is “the activity of converting or conditioning tangible personal property by changing the form, composition, quality, combination, or character of the property for ultimate sale at retail or for use in the manufacturing of a product to be ultimately sold at retail or affixed to and made a structural part of real estate located in another state.”
 - Example: Contractor constructs a foundation for a machine press for use in industrial processing by Manufacturer. The foundation is exempt from sales and use tax.

Michigan–Statutory Exemptions

Property to be Affixed to and Becoming a Structural Part of Real Estate Located Outside Michigan (Use Tax Only)

- Effective January 1, 2005, property that is purchased by a contractor for the purpose of constructing, altering, repairing, or improving real estate for others and that is affixed to and made a structural part of real estate located in another state is exempt from use tax.
- However, there is no corresponding sales tax exemption. Therefore, when a contractor purchases property for affixation in another state from a Michigan retailer, absent another reason to claim exemption, the contractor has no basis to claim a sales tax exemption. Even if the purchaser makes an invalid claim of exemption, the retailer is not liable unless it is involved in fraud

MICHIGAN

MANUFACTURER
/CONTRACTORS

Michigan–Manufacturer/Contractors

Manufacturer/Contractor is a person who manufactures, fabricates or assembles tangible personal property and subsequently affixes its product to the real estate of others.

- ***Use Tax Treatment***

If a manufacturer/contractor

- maintains an **inventory** of its product(s) available for sale to others, OR
- makes its product available for sale to others by **publication** or **price list**,
- the use tax base for products withdrawn from inventory and affixed to realty in Michigan is **finished goods inventory value** as outlined in 26 CFR 1.471-11. The manufacturer/contractor's equipment and supplies will qualify for the industrial processing exemption if they are used in the industrial process.
- **However, tools used at the construction site do not qualify for exemption unless used to mix, blend, etc.**

Michigan–Manufacturer/Contractors

If a manufacturer/contractor:

- does **not** maintain an **inventory** of its product available for sale to others, AND
- does **not** make its product available for sale to others by **publication** or **price list**,
- the use tax base for products withdrawn from inventory and affixed to realty in Michigan is the sum of the cost of **direct materials** and **direct labor** to manufacture, fabricate, or assemble the property. *The components of direct materials and direct labor are discussed in 26 CFR 1.471-11 and the related statutes.*
- The **manufacturer/contractor's equipment and supplies do not qualify for the industrial processing exemption.**
- The words **fabricate**, **manufacture**, and **manufacturer** are defined by statute at MCL 205.93a(5). The Department defines **assemble** as to gather into a group, or collect or fit or put together parts.

Michigan–Manufacturer/Contractors

Direct Labor

Direct labor pertains to staff directly engaged in production, including manufacturing or fabricating (including mixing, combining, or blending) at the job site prior to affixation, operating fabricating machines, and in-process material handling.

- Costs of direct labor include but are not limited to:
- Wages (basic, overtime, and shift differential)
- Fringe benefits (includes voluntary employee benefits association (VEBA) payments, union dues, clothing & laundry reimbursements, meals and meal allowances, and payments directly incurred for production employees, sick leave pay, vacation and holiday pay)
- Accident, health, long-term disability, and life insurance plans
- Bonuses, commissions, stock bonuses, profit sharing
- Workers' compensation (severance pay, supplemental unemployment benefit plan payments)
- Pension and retirement
- Payroll taxes
- Any other payment incurred on behalf of employees directly engaged in production

Michigan–Manufacturer/Contractors

- Direct labor **does not include** staff performing shipping and receiving, shop supervision, or maintenance and repair functions.
- In addition, direct labor to cut, bend, assemble or attach **at the job site** in Michigan is specifically exempted from the use tax base by statute.
- However, these costs would be part of the cost of labor to manufacture if performed at the taxpayer’s location or other non-job site location.
- In general, the cost of labor to “cut, bend, or assemble ... property at the site for affixation” relates to the cost of labor at the job site to make minor adjustments, alignments, alterations and other changes which are necessary in order to affix the property to real estate in Michigan.

Examples:

- Incidental mixing such as the mixing of mortar and tinting of paint at the job site is not be included in the use tax base
- Costs of labor incurred at the job site in Michigan (other than to cut, bend, assemble or attach) which fall within the definition(s) of **manufacture** and/or **fabricate** are included in the use tax base such as costs of labor at the job site for mixing, combining or blending prior to affixation of property will be included in the use tax base

Michigan–Manufacturer/Contractors

Direct Materials

- Direct materials include raw materials, supplies entering into or consumed in connection with the product, and costs incurred to move the material to the point of manufacturing.
- The cost of a sub-processing activity by an outside party is also included in the cost of material for determining the use tax base. It does not matter if the sub- processing occurs before or after the transfer of ownership to or possession by the manufacturer/contractor

Michigan–Manufacturer/Contractors

Finished Goods Inventory Value

- Finished goods inventory value is calculated according to the full absorption method of inventory valuation for manufacturers as described in 26 CFR 1.471-11.
- In general, this valuation method includes all direct production costs, defined as components of either direct material or direct labor.
- Indirect production costs are included **only to the extent** that such costs are incident to and necessary for production or manufacturing operations or processes.
- These indirect production costs include but are not limited to:
 - repairs and maintenance
 - Utilities
 - Rent
 - indirect materials and supplies
 - tools and equipment that are not capitalized
 - costs of quality control and inspection
 - indirect labor and production supervisory wages
 - other employee benefits

Michigan–Manufacturer/Contractors

Finished Goods Inventory Value

- Finished goods inventory value generally does not include:
 - Marketing
 - research and development
 - Sales
 - general and administrative expenses
 - officer salaries that are incident to and necessary for the taxpayer’s activities taken as a whole rather than incident to and necessary for production or manufacturing operations or processes
 - costs of labor to cut, bend, assemble or attach tangible personal property at the job site are also excluded from finished goods inventory value

Michigan–Manufacturer/Contractors

Inventory

- The following criteria are used to determine if a taxpayer maintains an inventory of its product(s) available for sale to others:
 - **1.)** The inventory must be similar to the product that it affixes to realty.
 - For example, a countertop manufacturer/contractor might have a retail inventory of shelving that it sells to walk-in customers, though it makes custom countertops to order. This fact would not require the contractor to pay use tax on the finished goods inventory value of the installed countertops.
 - **2.)** The inventory does not have to be a completely finished product to meet the definition of a product that is available for sale to others.
 - For example, a contractor that fabricates and erects structural steel could have bar steel inventory in stock that it will bore out for retail sale at a customer's request. The product sold is similar to the product erected, even though not in a finished state.
 - **3.)** The retail sale of related products should be more than de-minimus.
 - **4.)** A book or tax accounting inventory is not a requirement, only the existence of an actual physical inventory.

Michigan–Manufacturer/Contractors

Price List

- A numerical and/or alphabetical enumeration of goods, wares, merchandise items or services, quoting wholesale and/or retail prices and presented, maintained or otherwise displayed in any written or electronic form and which represents the final cost (price) of the finished product. A price list includes, but is not limited to, printed cards or sheets, or pricing available within a database or through an Internet website.
- **Note:** A price list does not include a preliminary price quote or general advertisement that is (or presents) merely an estimate of the approximate purchase price or cost of the product or which is not made available to the public or potential customers.
 - For example, an advertisement, brochure or pamphlet that contains general (base) floor plan layouts that a purchaser can choose from which a customized product can be built does not constitute a “price list”

Michigan–Manufacturer/Contractors

Publication

- Includes, but is not limited to, a **catalog**, **sales pamphlet** and **sales handbill** or pricing on an Internet website.
- **Catalog:** A bound, stitched, sewed or stapled book or pamphlet, or document maintained in electronic format (e.g., hard drive or Internet), containing a list and description of goods, wares, merchandise or services with specific information, with or without a price.
- **Sales Pamphlet:** A printed work concerning goods, wares, merchandise or services, consisting of two or more sheets, stapled, sewed or stitched, with or without a price.
- **Sales Handbill:** A printed single sheet (sometimes called a circular or dodger) intended to be circulated and concerning goods, wares, merchandise or services.
- **Note:** A publication or price list must reflect the amount charged for tangible personal property and not an installed total. It also must reflect a finished goods price (not cost of raw material).

Michigan–Manufacturer/Contractors

Example 1:

- A manufacturer/contractor enters into a contract to build a house. In its workshop, the manufacturer/contractor cuts and assembles roof trusses. The trusses are later transported to the job site and used to construct the house. The use tax base of the trusses is the cost of materials plus the cost of labor to cut and assemble them in the workshop (to the extent that the cutting falls within the definition of **manufacture** and/or **fabricate** and/or the assembly of the trusses falls within the definition of **assemble**.) However, the cost of labor incurred at the job site to cut, bend, assemble, or attach the trusses to the real estate are not included in the use tax base.

Michigan–Manufacturer/Contractors

- **Example 2:**

A custom cabinetmaker enters into a contract to build and install cabinets in an office building. The cabinet doors are constructed at the cabinetmaker's off-site workshop. The completed cabinet doors and other materials are brought by the cabinetmaker to the job site where the cabinetmaker completes the construction and assembly of the cabinets. The use tax base of the cabinets is equal to (i) the cost of the materials; (ii) all off-site direct costs of labor to construct the cabinet doors; and (iii) all on-site direct costs of labor to construct and complete the cabinets (to the extent that construction and completion of the cabinets at the job site falls with the definition(s) of **manufacture** and/or **fabricate** under MCL 205.93a(5)). Any direct costs of labor incurred at the job site to cut, bend, assemble, or attach the cabinets to the real estate are not included in the use tax base.

Michigan–Manufacturer/Contractors

Example 3:

- A manufacturer/contractor fabricates and installs steel beams. Engineering/detailing costs that are related to manufacturing should be included in direct material costs under both tax-treatment options. This would include the cost of blue prints, certification tests, and architectural design costs, whether done in-house or by an outside company. These costs would be part of the direct material costs because they are necessary to determine what material to purchase for the job (what strength or grade of steel).

Example 4:

- An asphalt company manufactures asphalt that is sold at retail and consumed in contracts. When the company consumes this asphalt, use tax is due on the inventory value. No distinction is made between **special blends** not sold at retail and regular blends. Use tax is due on the inventory value of both

Michigan–Manufacturer/Contractors

Example 5:

- An asphalt manufacturer/contractor uses the asphalt removed from the current road bed in the production of the new asphalt. The cost of transporting this recycled asphalt product to the asphalt plant should be included in direct material costs as freight-in.
- This computation would also include depreciation, oil, gas and maintenance of the roto mill, as well as the labor costs of the roto mill operator. These costs would be included under both tax-treatment options. The labor cost of the truck driver transporting the product to the plant would be a part of finished goods inventory value but would not be a direct labor cost

Michigan–Manufacturer/Contractors

Other Activities of Manufacturer/Contractors

- A manufacturer/contractor can be engaged in more than one distinct business activity. In these situations, the use tax base would depend on the circumstances for that particular part of the business. The availability of the industrial processing exemption for equipment and utilities would vary as well.

Example 1:

- ABC Company purchases kitchen cabinets for retail sale and acts as the contractor when installing the cabinets. ABC's use tax base when acting as the contractor is the material cost. In this situation ABC Company is acting as a retailer and is not entitled to the industrial processing exemption.

- **Example 2:**

ABC Company also manufactures a custom cabinet for the bathroom and maintains an inventory of its manufactured cabinets. If it needs additional cabinets, it purchases a standard cabinet for installation from an outside source. Its cost, when acting as a contractor, is the **finished goods inventory value** on the cabinets that it manufactured and material cost (at the purchased price which includes freight) on the cabinets that it purchased. ABC Company is entitled to the industrial processing exemption on the cabinets manufactured for retail sale or used in contracts.

Michigan–Manufacturer/Contractors

Example 3:

- By word of mouth, some customers have discovered that ABC Company has the equipment to manufacture hardwood flooring.
 - This specialty flooring is not available for sale through a publication or price list.
 - Each floor is custom made to the customer’s specifications.
 - The use tax base when ABC Company affixes the flooring to realty in Michigan is the direct cost of material and the direct cost of labor to manufacture.
 - The inventory of the wood products, including the standard cabinets that it either manufactured or purchased, does not constitute inventory for the flooring when determining the use tax base for the company when it affixes the flooring to realty in Michigan
 - Furthermore, ABC Company is not entitled to the industrial processing exemption if it affixes all the custom hardwood flooring that it manufactures to real estate in Michigan.
 - However, if it makes retail sales of the custom flooring, it is entitled to the exemption based on a percentage determined by comparing the retail sales to the contract sales. It would also be entitled to the industrial processing exemption for the hardwood flooring if installed to real estate located in another state.

Michigan–Manufacturer/Contractors

Example 4:

- The use tax base for a contractor who withdraws gravel from its own pit for use in a paving contract and not for resale would be zero. The labor to extract would not be included. This taxpayer would be considered a contractor, not an extractor, since the gravel extracted is not for resale.

Example 5:

- If gravel is withdrawn from the pit of another for use in a contract, the cost for use tax purposes would be the amount paid to the pit owner for the material. The labor to extract would not be included. In this case, the taxpayer would be considered a contractor, not an extractor.

Example 6:

- If a taxpayer bought a sand hill and used the sand to make glass to install in a building, the use tax base would be the cost of the material. This taxpayer is a manufacturer/contractor, not an extractor. If the taxpayer also sold sand at retail, it would also be an extractor

Michigan–Manufacturer/Contractors

Example 7:

- If an extractor/manufacture/contractor maintained a standard inventory of aggregate for sale to others, the use tax base when using aggregate in performance of a contract would be the finished goods inventory value – whether extracted from the extractor/manufacture/contractor’s own pit or the pit of another.
- For a Manufacturer/Contractor who affixes its product to real estate of others located in Michigan, and:
 - does not maintain an inventory of its product available for sale to others
 - OR**
 - does not make its products available for sale to other by publication or price list, the use tax base will be determined in accordance with MCL 205.93a(1)(g), not the finished goods inventory value.

Michigan–Manufacturer/Contractors

- The price is the sum of the materials cost of the property and the cost of labor to manufacture, fabricate, or assemble the property affixed to the real estate in Michigan, but not the cost of labor to cut, bend, assemble or attach the property at the site for affixation to real estate in Michigan (explicitly excluded by statute).
- Material cost is the invoice price of raw materials and supplies entering into or consumed in connection with the contract and other necessary charges incurred in acquiring possession of the goods. Material costs includes the cost of direct material.
- Cost of labor is the cost of direct labor and does not include payments made for shipping, assembly, loading and unloading or otherwise transporting the product to the job site. The cost of direct labor to **manufacture** or **fabricate** tangible personal property affixed to real estate located in Michigan is included in the use tax base regardless of whether the activity occurs off-site or at the job site. However, the cost of direct labor to **assemble** the product is only included in the use tax base if the costs are incurred off-site

Michigan–Manufacturer/Contractors

Transformational Brownfields

- The manufacture of a product identified in section 3a(1)(f) or (g) of the Use Tax Act is exempt from use tax if used for eligible activities described in section 2 of the Brownfield Redevelopment Financing Act on **eligible property** that is included in a **transformational brownfield plan**, to the extent that the product will be affixed to and/or made a structural part of the real property or **infrastructure improvements** included within the transformational brownfield plan. “Eligible property”, “infrastructure improvements”, and “transformational brownfield plan” mean those terms as defined in section 2 of the Brownfield Redevelopment Financing Act.
- **Note:** 2017 PA 48 requires the tangible personal property to be affixed to “and” made a structural part of the “real property or infrastructure improvements” included within the transformational brownfield plan the real estate. 2017 PA 49 requires the tangible personal property to be affixed to “or” made a structural part of the “improvements to real property” included within a transformational brownfield plan”

Michigan–Manufacturer/Contractors

Tangible personal property that becomes:

- **1.)** an ingredient part or component part of the finished product to be ultimately sold at retail
- OR**
- **2.)** an ingredient part or component part of tangible personal property that is permanently affixed to and made a structural part of real estate located in another state, is eligible for an industrial processing exemption. If the product is available for ultimate sale at retail to others, the industrial processing exemption applies even if the manufacturer/contractor removes the product from inventory and affixes it to (and makes it a structural part of) the real estate of another so long as the real estate is located **outside** of Michigan. The industrial processing exemption is limited to the percentage of exempt use to total use determined by a reasonable formula or method approved by the Department. The formula or method used does not have to be preapproved by the Department, but it must reasonably reflect the percentage of exempt use to total use.

Michigan–Manufacturer/Contractors

- For example, the manufacturer/contractor may prorate exempt use based on industrial processing relating to tangible personal property affixed to (and becoming a structural part of) real estate located in another state versus real estate located in Michigan.
- Tangible personal property permanently affixed and becoming a structural part of real estate ***in this state*** is not eligible for the industrial processing exemption. If the manufacturer/contractor sells its products in retail transactions, sales tax on the sales prices of the products must be collected and remitted to the state unless the purchaser has a valid exemption.

Michigan–Manufacturer/Contractors

TruGreen Ltd. P’ship v. Dept. of Treasury , Mich. Ct. App., No. 344142, opinion 7/29/21 .

- The purchase of fertilizer, insecticide and equipment that could be used in farming, TruGreen Limited Partnership and other Michigan lawn care companies can’t qualify for the broad sales and use tax break available to agricultural producers, the Michigan Court of Appeals rule
- The opinion denied Memphis-based TruGreen a roughly \$1.2 million refund on taxes it remitted over a four-year period on the purchase of equipment and products used to spiff up customers’ lawns and shrubbery. The split decision found that while the company performed some of the actions laid out in the tax break statute, such as tending to “things of the soil,” the company wasn’t participating in the intended industry: agriculture.
- The grass TruGreen “plants and tends is decorative, and the work it does is unrelated to crop cultivation or agriculture in general,” Judge Elizabeth L. Gleicher wrote in her opinion joined by Judge Douglas B. Shapiro. “Considered within its contextual milieu, the term ‘things of the soil’ pertains to the products of farms and horticultural businesses, not blades of well-tended grass.”
-

Michigan–Manufacturer/Contractors

Brusky v. Dep't of Treasury, No. 355670 (Mich. Ct. App. Jan. 13, 2022)

- The Michigan Court of Appeals recently affirmed a lower court decision holding that a taxpayer was making retail sales of tangible personal property and was liable for sales tax on its delivery charges.
- The taxpayer transported aggregate materials, such as sand or gravel, via truckload for customers' construction projects. When it purchased the materials, the taxpayer provided a resale certificate. The taxpayer's customers were billed one lump-sum for materials, delivery charges, and tax.
- The taxpayer calculated and collected sales tax only on the materials and did not remit tax on the delivery charges. On audit, Treasury determined there was a deficiency related to the delivery charges. The taxpayer protested. After the court of claims ruled in Treasury's favor, the taxpayer appealed.
- Under Michigan law, the sales tax base for "... from the seller to the purchaser." **all persons engaged in the business of making sales at retail" includes "delivery charges," so long as such charges are incurred "before the completion of the transfer of ownership of tangible personal property**

Michigan–Manufacturer/Contractors

Brusky v. Dep't of Treasury, No. 355670 (Mich. Ct. App. Jan. 13, 2022)

- The taxpayer's position centered its argument that it was not making sales at retail.
- The taxpayer first asserted it was not making sales at retail but was acting as a "purchasing agent" for its customers.
- However, the court noted that even in the broadest definition of "agent," the principal must control the activities of the agent. There was no evidence that the customers had any control over where aggregate was purchased, or the delivery routes used to deliver the materials.
- Further, the taxpayer's use of an exemption certificate to purchase the aggregate indicated it considered itself a retailer.
- The taxpayer next tried to argue because its primary business activity was not making retail sales it was not subject to sales tax on delivery charges. The court firmly rejected this position, noting that the Michigan sales tax law contains no requirement that a person be primarily engaged in the business of retail sales to be subject to tax.
- Finally, the taxpayer asserted that its primary business was a service (the procurement and delivery of aggregate), and it was not subject to sales tax under the incidental-to-services test of *Catalina Marketing Sales Corp v Dep't of Treasury.* In the court's view, the *Catalina* case was not applicable because the Legislature had expressly mandated that delivery services related to sales of tangible personal property were subject to sales tax.

OHIO COMMERCIAL ACTIVITY TAX (CAT)

Ohio – Commercial Activity Tax (CAT)

Basics of the Tax

- The CAT is a broad-based, low rate tax on the privilege of doing business in Ohio that is measured by a taxpayer's taxable gross receipts.
- **Taxpayers Include:**
 - Individuals
 - Trusts
 - Disregarded entities
 - Associations
 - Joint ventures
 - Partnerships
 - Limited liability companies
 - Pass-through entities
 - C-Corporations
 - S-Corporations

Ohio – Commercial Activity Tax (CAT)

Basics of the Tax

- **Not Covered by the Tax:**

- Non-profit organizations
- Most governmental entities
- Some public utilities
- Insurance companies that pay the insurance premiums tax
- Financial institutions that pay the financial institution tax and certain affiliates of financial institutions
- Businesses with less than \$150,000 of taxable gross receipts (unless they are part of a "consolidated elected taxpayer" or "combined taxpayer group")

Ohio – Commercial Activity Tax (CAT)

Basics of the Tax

- **Nexus** - A person has “bright-line presence” in this state if any one of the following applies at any time during the calendar year:
 - The person has at least \$50,000 of either property or payroll in this state; OR
 - Taxable gross receipts sitused to Ohio are at least \$500,000; OR
 - 25% of the person’s total property, total payroll or total gross receipts within this state; OR
 - The person is domiciled in this state as an individual or for corporate, commercial, or other business purposes
 - A person meeting one of the nexus standards must also have at least \$150,000 in taxable gross receipts sitused to Ohio during the calendar year to be subject to the CAT.
- **Gross Receipts** - The total amount realized by a person, without deduction for the cost of goods sold or other expenses incurred, from activities that contribute to the production of gross income.

Ohio – Commercial Activity Tax (CAT)

Basics of the Tax

- Exclusions from Gross Receipts
 - Interest (except from credit sales)
 - Dividends and distributions or distributive or proportionate shares
 - Employee Compensation
 - Receipts in excess of an agent's commissions, fee, or other remuneration
 - Sales or use taxes
 - Certain excise taxes paid
 - Qualifying distribution center receipts
 - Motor fuel
 - Cash discounts allowed and taken
 - Returns and allowances
 - Bad Debts
 - Amount realized from the sale of an account receivable

Ohio – Commercial Activity Tax (CAT)

Situsing of Gross Receipts

- Things to consider when situsing gross receipts from the sale of tangible personal property:
 - Whether the buyer or seller of the property arranges or provides the transportation does not change how the gross receipts are sitused.
 - Use of common carriers does not change how the gross receipts are sitused.
 - Location of title transfer does not control.
 - Transfer of risk of loss does not control.
 - Generally, cannot “*look-through*” to determine situs

Ohio – Commercial Activity Tax (CAT)

Situsing of Gross Receipts

- As a general rule, gross receipts from services are sitused based on the proportion of the purchaser's benefit received in Ohio with respect to what was purchased compared to the purchaser's benefit everywhere.
 - Unless otherwise provided, the physical location where the purchaser ultimately uses or receives the benefit is paramount in determining the proportion of the benefit received in Ohio.
- Ohio administrative code **5703-29-17**
 - Provides situsing rules for 53 enumerated services.
 - Can be used as guidance for services that are similar to those enumerated services.

Ohio – Commercial Activity Tax (CAT)

Types of Taxpayers

- Combined Taxpayer Groups
- Consolidated Elected Taxpayer Groups
- Single Entity Taxpayers

Combined Filing

- **Mandatory** for all persons, other than excluded persons, having more than 50% of the value of their ownership interest owned or controlled
- Only entities with nexus via a bright-line presence test
- Persons who do not have nexus with the state of Ohio may nevertheless be “common owners,” but are not required to register as part of group for the CAT
 - Nexus is applied on a person-by-person basis
- Taxable Gross Receipts are calculated in the aggregate
 - Cannot exclude receipts between members of the group

Ohio – Commercial Activity Tax (CAT)

Consolidated Filing Election

- The group elects to include all persons, including excluded persons, having at least 50% or 80% of the value of their ownership interests owned or controlled.
- Taxpayer agrees to waive any nexus challenges.
- Registration must include excluded persons.
- Exclude taxable gross receipts between members
- Binding for eight (8) consecutive calendar quarters
- Automatically renews unless the taxpayer notifies ODT of its decision to cancel the election before the end of the 8 consecutive quarters.
- May either include or exclude all non-U.S. entities or persons

Ohio – Commercial Activity Tax (CAT)

CAT Tiered Structure

Annual Gross Receipts	Minimum Tax Liability	CAT Liability
\$0 – \$150,000	n/a	n/a
\$150,001 – \$1,000,000	\$150	n/a
\$1,000,001 – \$2,000,000	\$800	0.26% on receipts > \$1 million
\$2,000,001 – \$4,000,000	\$2,100	0.26% on receipts > \$1 million
Over \$4,000,000	\$2,600	0.26% on receipts > \$1 million

Ohio – Commercial Activity Tax (CAT)

- **Agency Exclusion - R.C. 5751.01(F)(2)(I)**
 - The definition of “gross receipts” excludes property, money, and other amounts received or acquired by an agent on behalf of another in excess of the agent’s commission, fee, or other enumeration.
- **“Agent” Defined – R.C. 5751.01(P)**
 - An “agent” means a person authorized by another to act on its behalf to undertake a transaction for the other, including [specific examples]”
 - See, *Willoughby Hills Dev. & Dist. v. Testa*, 155 Ohio St.3d 276 (2018) (denying agency exclusion to gas distributor)

Ohio – Commercial Activity Tax (CAT)

CAT Agency Exclusion

- Contract Language
 - Presumption that there is no agency relationship if it is not expressly stated in the contract - O.A.C. 5703-29-13(C)(2)(a)
- Document Everything!
 - Tax Dept may look beyond contract even if there is express language. O.A.C. 5703-29-13(B)(2).
- TC Opinions 08-0001, -0007, -0011, -0012: Exclude if:
 - Contract expressly states that the General Contractor is Owner's agent, and not Subcontractor's agent; AND
 - General Contractor is acting in the Owner's best interests; AND
 - General Contractor is acting as a conduit for payments to the Subcontractor

Other Factors

- Party controlling manner and means of doing work
- May agent bind and/or cause the principal liability?

Ohio – Commercial Activity Tax (CAT)

Agency Example – O.A.C. 5709-23-13

- A general contractor enters into a costs-plus contract with a property owner for the general contractor to construct an office building.
- Under the terms of the contract, the owner agrees to pay the general contractor for work completed by the subcontractors at **cost plus a 5% fee.**
- The general contractor is **required to act in the owner's best interests** with respect to cost issues.
- The general contractor, when bidding out the work to subcontractors, has an agreement in writing with the subcontractors that states that the **general contractor is acting as the owner's agent and not as an agent of the subcontractor.**

Ohio – Commercial Activity Tax (CAT)

Agency Example – O.A.C. 5709-23-13

- **The general contractor acts as a conduit** with regard to any payments made to the subcontractors, in that the general contractor remits monies received from the owner to the subcontractors, provided that certain conditions are met.
- Accordingly, the general contractor may exclude the money that the general contractor receives from the owner to pay the subcontractors from its gross receipts.
- However, the 5% fee retained by the general contractor would be included in its calculation of gross receipts for purposes of the commercial activity tax

Ohio – Commercial Activity Tax (CAT)

Willoughby Hills Development and Distribution, Inc. v. Testa

- On July 5, 2016, the BTA issued its first decision interpreting the CAT’s so-called “agency exclusion”
- R.C. 5751.01(I) provides: (I) Property, money, and other amounts received or acquired by an agent on behalf of another in excess of the agent's commission, fee, or other remuneration;
* * *
- (P) ‘Agent’ means a person authorized by another person to act on its behalf to undertake a transaction or the other, including any of the following: * * * (2) A person retaining only a commission from a transaction with the other proceeds from the transaction being remitted to another person;” (Emphasis added).

Facts

- The taxpayer was a gasoline distributor that bought gasoline and various fuel products from Sunoco Inc. and then resold the items to various service stations in Ohio.
- The taxpayer asserted that many of the terms in its distributor agreement with Sunoco reflected Sunoco’s control over taxpayer’s actions and, therefore, reflected an agency relationship.

Ohio – Commercial Activity Tax (CAT)

Willoughby Hills Development and Distribution, Inc. v. Testa

RULING

- The facts and circumstances did not support an agency relationship.
- The taxpayer must be “authorized” by Sunoco “to act on its behalf to undertake a transaction for Sunoco.”
- The taxpayer’s sale of the gasoline and fuel products to a particular retailer was not undertaken “on behalf” of Sunoco. The taxpayer was “generically required to act in Sunoco’s ‘best interests’ by complying with company ‘minimum standards,’ ” but the taxpayer maintained control over its own employees and equipment.
- The BTA noted that no testimony was provided by a Sunoco witness to evidence an agency relationship and thereby negate the contractual language.
- The Ohio Supreme Court affirmed the BTA’s decision on November 7, 2018

Ohio – Commercial Activity Tax (CAT)

Receipts from Agency Relationships:

- Amounts acquired by an agent on behalf of another in excess of the agent's commission, fee, or other remuneration are excluded from taxable gross receipts. However, the **Department's position is that a lack of agency is presumed unless the agency relationship is explicitly stated in the contract.** There are several cases pending at the BTA in which a taxpayer is seeking to establish that an agency relationship exists:

Apple, Inc. v. McClain (BTA Case No. 2020-55)

- Taxpayer argued that it is entitled to exclude a portion of its receipts from sales of various digital products such as eBooks, Apps, music, news service, and movies sold through its App Store and other digital content stores.
- Specifically, Apple argues that 70% of the receipts from those sales should be excluded because Aramark acted as an agent of the developers of those products in making the sales. Apple also argues that certain of its other sales were made to Qualified Distribution Centers such as Best Buy and PC Connection and thus should be excluded from taxable gross receipts to the extent those goods were ultimately sold outside Ohio. The case is scheduled for a hearing April 4, 2022.

Ohio – Commercial Activity Tax (CAT)

Cavaliers Holdings, LLC v. McClain (BTA Case No. 2020-55)

- The taxpayer enters into event agreements with promoters for events at Q Arena in Cleveland.
- The taxpayer enters into fixed fee contracts or formula-based fee contracts, which include a minimum fixed fee plus a percentage of receipts from ticket sales.
- In exchange, the taxpayer provides a lease to use the arena as well as ticket selling and other ancillary stadium services.
- For both types of contracts, the **Commissioner assessed CAT on all ticket sales (not just the rental fee).** The taxpayer is arguing that for fixed fee events, only the rental fee is included in taxable gross receipts. For formula-based contracts, the taxpayer argues that only the portion of ticket sales they retain after paying promoters is included in taxable gross receipts.
- In each case, the taxpayer argues that it did not realize gross income equal to 100% of the ticket proceeds. Alternatively, the taxpayer argues that it is entitled to exclude amounts that it received as an agent under O.R.C. § 5751.01 (F)(2)(I). **The Commissioner takes a broader interpretation of gross receipts, and argues that the taxpayer does not qualify as an agent because the contract does not explicitly name the taxpayer as an agent.**
- The case was heard on December 8, 2021, waiting for ruling.

SALES/USE TAX
AUDIT PREPAREDNESS
BEST PRACTICES

Sales/Use Tax Audit preparedness

Best Practices

Project Bidding and Budgeting

- Fully understand nature of job/contract from beginning to end – before bidding
- Certain projects may carry additional exemptions:
 - Manufacturing
 - Port Authority contracts
 - Government contracts
- Understand treatment of the particular contract in the state where work will be performed
- Understand sales tax and use tax paid to vendors and reimbursed by contractee vs. sales tax “collected” from contractee and remitted by contractor
- Does job include any temporary components, business fixtures, or tangible personal property?
- Identify sales tax collection requirements, temporary components, business fixtures, or tangible personal property and include applicable sales tax in bid
- Create job aid for bidders and estimators to ensure tax included correctly in bid

Sales/Use Tax Audit preparedness

Best Practices

Invoicing

- Sales tax licenses required if selling tangible personal property/business fixture
- Collection and remittance vs. reimbursement of cost incurred
- If billing sales tax, separately state sales tax on invoice
- Use supporting information with AIA documentation

Purchasing and Accounts Payable

- Purchase orders issued indicating taxable or non-taxable
- Separate taxable and non-taxable accounts with vendors
- Know when to issue exemption certificate to vendor
- Review invoices carefully for sales tax included or not included
- In Ohio, materials purchased for temporary or business fixture components of job are purchases for resale and Ohio sales tax should be collected from contractee
- “Short-pay” invoice if warranted

Sales/Use Tax Audit preparedness

Best Practices

General Best Practice

- Know your customers
- Understand the costs and budgeting process
- Understand the projects what is real property versus tangible personal property
- Sales Tax Exemptions – Entire project will not likely qualify for exemption
- Procure and maintain properly completed exemption certificates
- Documentation is the key **Document, Document, Document**
- Use AIA documents
- Capture sales tax paid to vendor separately, if possible
- Create sales tax payable and use tax accrual accounts by state
- Assume that you will be audited at some point, have “**audit ready**” files
- Use flow charts/matrices to create a repeatable process

Taxpayer Documentation – Best Practice

- **What Documentation is required?**
 - **General Ledger** — This can include the contracts that the contractor is obligated to follow and the discharge of the liability as the job progresses and billings are made.
 - **Books of Original Entry** — A purchase journal and cash disbursement journal can show material purchases to inventory or specific jobs.
 - **Sales Journal** - Billings, over-the-counter sales, time and material contracts and fixture sales prices.
 - **Supplemental Records** — Items can include a contract register that includes specifics of the job, such as owner name, job location, project description, contract type, contract amount and completion dates.
 - **Cost Journal** - Material cost, labor, overhead, sub-contract, etc.
 - **Requisition Journal** - Material and fixture drawdowns.
 - **Additional Supporting Documents** — These items can include billing details, AIA documents, job costs folders with plans and specifications, cost estimates, contract, purchase invoices, material drawdowns, time cards, paid invoices and applicable exemption certificates, pollution control certificates.

QUESTIONS AND ANSWERS

THANK YOU FOR
YOUR TIME AND
ATTENTION

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