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DEPARTMENT OF TREASURY
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LETTER RULING 2019-4

LR 2019-4. Sales and use tax liability of countertop manufacturer that subcontracts out the installation of the countertops.

You are a manufacturer/contractor that fabricates and installs countertops based on orders placed with retailers ("Retailers") by their customers ("Customers"). You perform these functions based on agreements ("Contracts") you have with these Retailers. Currently, you handle the installation of these countertops yourself, but you propose subcontracting the installation to third-party contractors ("Subcontractors") that you will hire for that purpose. The facts relating to the proposed process are described below:

- Customers place orders with Retailers for the installation of custom-made countertops and enter into separate agreements with the Retailers. The terms of those agreements are not disclosed to you.
- Retailers issue "purchase orders" to you detailing the materials and installation services required for the countertops ordered by the Customers.
- You manufacture the countertops based on the purchase orders you receive from Retailers.
- You issue purchase orders to the Subcontractors for their installation services.
- The Subcontractors are paid a flat fee for installation (per square foot), "tearouts" (per square foot) and service charges, plumbing, and zone charges at specified rates.
- Subcontractors pick up the countertops and install them at Customers' locations.
- The Contracts specify that title to the countertops pass from you to the Customers "upon installation" and not when Customers place their orders with the Retailers.
- You intend to claim a "sale for resale" and/or "industrial processing" exemption for the materials used in the manufacturing process, so no sales or use tax will be paid by you on your purchase (or use) of those materials.
- Upon successful installation and Retailers' receipt of signed Customer approval notices, Retailers pay you for the countertops (and installations) under the purchase orders.

Ruling Request. You request confirmation that you have "no Michigan Sales and/or Use Tax liability" on the materials you will use to manufacture the countertops that will be installed by your Subcontractors on the real property of the Customers. You also seek confirmation that you are eligible to claim the industrial processing exemption relating to these manufacturing activities.

Based on the facts you presented, there appear to be at least five transactions/events involved; some of which are taxable and some of which are not taxable. Each of these transactions/events are addressed separately.

1. ***Taxable Transactions/Events***

    - Sales to (purchases by) you of materials used in the manufacture of the countertops, including the base countertop material (e.g., marble, granite, quartz).
    - Consumption by you of the countertops you manufacture which are to be affixed to real estate by Subcontractors.[1]

2. ***Non-Taxable Transactions Events***

    - Orders placed by Customers with Retailers for the installed countertops.
    - Issuance of purchase orders by Retailers to you.
    - Services of Subcontractors on your behalf to install countertops by affixation to real estate.
    - Payments by Retailers to you under the purchase orders.

Applicable Law. The Michigan General Sales Tax Act ("GSTA") and the Michigan Use Tax ("UTA") Act are complementary tax statutes that generally levy a 6% tax on the sale or use of tangible personal property (e.g., materials) in Michigan. The sales tax is levied on all persons engaged in the business of making "sales at retail," which involve transactions in which "ownership of tangible personal property is transferred for consideration."[2]

A sale at retail does not include a sale "for resale."[3] Where the sale of tangible personal property is taxable, sales tax is measured by the "sales price" which is generally the "total amount of consideration, including cash, credit, property, and services, for which tangible personal property or services are sold."[4]

The UTA imposes tax on tangible personal property that is used, stored, or consumed in Michigan unless an exemption applies. For purposes of the use tax, contractors are considered the "consumers" of materials used, stored, or consumed by them when engaged in the business of constructing, altering, repairing, or improving real estate of others.[5] A "contractor" is a person

[1] For purposes of this Letter Ruling, the location of Customers' real estate is assumed to be in Michigan, so the applicability of MCL 205.94(1)(z) is not addressed.
[2] MCL 205.52(1).
[3] MCL 205.51(1)(b).
[4] MCL 205.51(1)(d).
[5] MCL 205.92(g)(i): "a person is a consumer of tangible personal property, and therefore liable for use tax, if the person is "acquiring tangible personal property [and is] engaged in the business of constructing, altering, repairing, or improving the real estate of others." See also Mich Admin Code, R 205.8.

directly engaged in the business of constructing, altering, repairing, or improving real estate for others and includes a prime, general, or subcontractor.[6]

With few exceptions, contractors are liable for use tax (based on the purchase price)[7] on the property they use, store, or consume, even if that property was not purchased by the contractor but was acquired from another.[8] However, the contractor's obligation to remit use tax is satisfied if sales tax is due and paid on the property at the time of purchase in a retail sale.[9] For example, the contractor may retain a copy of the customer's sales invoice from the retailer separately stating the sales tax to demonstrate that sales tax was due and paid on the property.

A "manufacturer" is a person who "manufactures, fabricates, or assembles" tangible personal property.[10] When a person is both the manufacturer of tangible personal property and the contractor that affixes that tangible personal property to real estate, that person constitutes a "manufacturer/contractor" regarding that tangible personal property.[11] Under certain conditions, a person may still qualify as a manufacturer/contractor even if that person subcontracts out the affixation (installation) work to another contractor.[12] The use tax base applicable to a manufacturer/contractor depends upon whether the manufacturer/contractor maintains an inventory of its product that is available for sale to others or makes its product available for sale to others by publication or price list.[13]

A manufacturer/contractor may claim an industrial processing exemption under the UTA for tangible personal property it uses or consumes for industrial processing in connection with its product *only* if the product is either ultimately sold at retail or is affixed to and made a structural part of real estate located in *another state*.[14] The industrial processing exemption is limited to the

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[6] Mich Admin Code, R 205.71.

[7] MCL 205.92(f). See also RAB 2016-18.

[8] Under MCL 205.94ee, a contractor is not liable for use tax for storing, using, or consuming property acquired from another person so long as: (i) the property was *purchased* by that other person; (ii) that other person is *not exempt* from the tax imposed under the GSTA or the UTA, and; (iii) the property was acquired by the contractor for the *sole purpose* of affixing the property to real estate on behalf of that other person.

[9] MCL 205.94(1)(a); RAB 2016-18.

[10] MCL 205.93a(5)(m).

[11] MCL 205.93a(1)(f)-(g). See also RAB 2016-24 (Use Tax Base of Tangible Personal Property Affixed to Real Estate by a Manufacturer/Contractor or other Contractor).

[12] See "Miscellaneous Questions and Answers" section of RAB 2016-24 which states, under Q&A #11: "If a manufacturer/contractor bills 'time and material,' but has a subcontractor perform the actual affixation of the product to realty in Michigan, the entity will still qualify as a manufacturer/contractor and will be liable for the use tax because the subcontractor was never billed for the material." See also footnote 16 in RAB 2016-24, which explains: "[I]f materials are billed to the subcontractor, the manufacturer/contractor is making a retail sale and does not qualify as a manufacturer/contractor with that transaction."

[13] MCL 205.93a(1)(f), (g); Revenue Administrative Bulletin ("RAB") 2016-24. You describe yourself as a "manufacturer/contractor," and it appears from the facts presented for purposes of the proposed process that you custom build the countertops that are installed by you (either directly or through a subcontractor) and no facts were presented to establish that you maintain an inventory of your countertops that are available for sale to others by publication or price list. Accordingly, the Department will treat you as a manufacturer/contractor subject to MCL 205.93a(1)(g).

[14] MCL 205.94o(1), (4)(a), (5)(a), (7)(a)-(b); RAB 2016-24. See also the industrial processing exemption from sales tax under MCL 205.54t which generally mirrors the language in the UTA except that it does not have an exception to the general rule (which prohibits industrial processing for property affixed to real estate) for affixation to real estate

percentage of exempt use to total use determined by a reasonable formula or method approved by the Department (which does not need to be pre-approved by the Department, but must reasonably reflect the percentage of exempt use to total use).[15]

Conclusions.

1. **Taxable Transactions/Events**

- ***Sales to (purchase by) you of tangible personal property used in the manufacture of the countertops, including the base countertop material (e.g., marble, granite, quartz)***. The sale to (purchase by) you of tangible personal property (e.g., marble, quartz, granite) to be used in the manufacture of the countertops under the "proposed process" are taxable as sales at retail by the seller.[16] Accordingly, the seller will have the obligation to remit sales tax on these transactions but may pass on the cost of the tax to you by charging it to you through the sales price.[17]

- ***Consumption by you of the countertops you manufactured which are to be affixed to real estate by Subcontractors***. As a manufacturer/contractor under MCL 205.93a(1)(g), you will generally owe use tax equal to the sum of the material costs of the product and certain direct labor costs.[18] Your use tax liability (e.g., for material costs) may be reduced by the amount of sales tax paid to or by the seller of the countertop materials for which you bear the burden of proof to demonstrate.

  If no sales tax was charged by the seller of the materials used by you to manufacture the countertops because you claimed "sale for resale" and/or "industrial processing" exemptions at the time of purchase, then you will owe use tax on the purchase price of those materials. You are not entitled to claim a resale exemption because the tangible personal property sold to you is not being purchased for resale, but will be used in the manufacture of countertops that will be affixed to real estate in Michigan. Likewise, you are not entitled to claim an industrial processing exemption because the tangible personal property sold to you is not going to be used to manufacture a product that will ultimately be sold "at retail" (there is no retail sale either between the Retailer and the Customers or between you and the Customers as title to the countertops does not pass to the Customers until *after* affixation to the Customer's real estate) or affixed to real estate outside Michigan.

  Under the "proposed process," Retailers act as contractors (general or prime) and contract with you as a subcontractor. In turn, you hire Subcontractors to complete the installation of the countertops manufactured by you by affixing them to real estate. Because you are not billing Subcontractors for time and materials, you will constitute a manufacturer/contractor, even though you will be subcontracting the

located outside Michigan. Because you are not making retail sales under the "proposed process," the analysis is limited to the application of the industrial processing exemption under the UTA.

[15] MCL 205.54t(2); MCL 205.94o(2). See also RAB 2016-24.

[16] For purposes of this Letter Ruling, the seller is assumed to be a retailer located in Michigan.

[17] MCL 205.73(1).

[18] See RAB 2016-24 for more detail on the specific costs included in the use tax base.

affixation work to them. Thus, the use tax liability will remain with you (as the consumer of the countertops) and will not pass to the Subcontractors performing the installation.

2. **Non-Taxable Transactions/Events**

- ***Order placed by Customers with Retailers for the installed countertops***. The transactions between Customers and Retailers do not constitute "sales at retail" as there is no transfer of ownership of tangible personal property for consideration taking place between them.[19] Rather, Retailers are acting as contractors (general or prime) under the "proposed process." Because there are no retail sales, no sales tax is due for these transactions and sales tax should not be charged by Retailers to their Customers.[20]

- ***Issuance of purchase orders by Retailers to you***. These transactions are between Retailers as contractors (general or prime) and you as a contractor (subcontractor to Retailers). These are not taxable transactions, so no sales or use tax would be due on them.[21]

- ***Services of Subcontractors on your behalf to install countertops by affixation to real estate***. As explained in this Letter Ruling, you retain the obligation to pay the applicable use tax as the contractor (e.g., manufacturer/contractor) deemed to be the "consumer" of the countertops despite your delegation of the actual affixation to real estate to Subcontractors. Thus, the "flat fees" paid by you to Subcontractors under the "proposed process" are not subject to sales or use tax.

- ***Payments by Retailers to you under the purchase orders***. Your use tax liability is established based on your role as the contractor consuming the countertops in their affixation to real estate. The payments to you under the terms of the Contracts and pursuant to the purchase orders are not subject to sales or use tax.

[19] As noted in this Letter Rulings, the Contracts specify that title passes to Customers upon installation of the countertops.

[20] If sales tax is, nonetheless, charged by Retailers and remitted to the Department on these transactions, then your use tax liability as a manufacturer/contractor may be extinguished in whole or in part. See MCL 205.94(1)(a). See also *Andrie Inc v Treasury Dep't*, 496 Mich 161, 170 (2014).

[21] See footnote 12 of this Letter Ruling. See also "Miscellaneous Questions and Answers" section of RAB 2016-24 which states, under Q&A #4: "We are a subcontractor. Our prime contractor received a job from a manufacturing company to do sheet metal work. The prime contractor subcontracted the work to us, and has furnished us with its use tax registration number and has stated that it will pay the use tax. We are supplying all of the materials and will be doing the actual work. Who is responsible for paying the tax on the job? A4: The contractor actually affixing the tangible personal property to the real estate is the taxpayer. The prime contractor in this case cannot assume the tax liability. The sales/use tax number is for the purchase of tangible personal property for resale or re-lease. After you have affixed the tangible personal property to real estate it is no longer tangible personal property, it is real property."