

## STATE OF MICHIGAN



JOHN ENGLER, Governor

**DEPARTMENT OF TREASURY**TREASURY BUILDING, P.O. BOX 15128, LANSING, MICHIGAN 48901  
DOUGLAS B. ROBERTS, State Treasurer**REVENUE ADMINISTRATIVE BULLETIN 1991-15**

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**SALES AND USE TAXATION IN THE CONSTRUCTION INDUSTRY**

RAB-91-15. This bulletin explains the Treasury Department's position regarding the application of sales and use taxes to the construction industry. This bulletin does not address the tax base for manufacturers who qualify as construction contractors or for contractors who manufacture, fabricate, or assemble property prior to affixing it to real estate.

**BACKGROUND**

Before May 1, 1970, a contractor performing a construction contract for an exempt entity, such as government, a church, or a nonprofit organization, was allowed to pass through to the supplier an exemption claim on behalf of the exempt entity. Public Acts 15 and 16 of 1970, effective May 1, 1970, limited this passthrough exemption to only those construction contracts performed for nonprofit hospital and nonprofit housing entities. Since May 1, 1970, construction contractors have been subject to sales or use tax when acquiring building materials for use or consumption in the performance of all other construction contracts. (See MCL 205.51(c); MSA 7.521(c) and MCL 205.94(1); MSA 7.555(4)(1).)

**THE LAW**

Section 1(c) of the General Sales Tax Act [MCL 205.51(c); MSA 7.521(c)] states as follows:

"Sale at retail" includes the sale of tangible personal property to persons directly engaged in the business of constructing, altering, repairing, or improving real estate for others except property affixed to and made a structural part of the real estate of a nonprofit hospital or nonprofit housing.

Section 2(g) of the Use Tax Act [MCL 205.92(g); MSA 7.555(2)(g)] states:

"Consumer" means the person who shall have purchased tangible personal property or services for storage, use or other consumption in this state and shall include a person acquiring tangible personal property when engaged in the business of constructing, altering, repairing or improving the real estate of others.

Finally, section 4(1) of the Use Tax Act [MCL 205.94(1); MSA 7.555(4)(1)] adds:

The tax levied shall not apply to:

\* \* \*

Property purchased by a person engaged in the business of constructing, altering, repairing, or improving real estate for others to the extent the property is affixed to and made a structural part of the real estate of a nonprofit hospital or a nonprofit housing entity

. . . .

## DISCUSSION

### Contractors

The statutes quoted above classify the contractor as the consumer in transactions involving tangible personal property which becomes real estate in the performance of a construction contract for others. As the consumer, the contractor must pay the sales or use tax due on the transaction when such tangible personal property is acquired in Michigan. This is true whether the construction takes place inside or outside of Michigan. (See 1979 AC, R 205.71(7).) The contractor cannot charge the tax to the other party to the contract because the contractor is using or consuming the building materials in constructing realty for others rather than reselling it at retail. (See Letter Ruling 80-3.) The contractor can, however, recover expenses incurred in performing the contract, including taxes paid on the building materials, by including the amount of such expenses in the total contract price.

The sales and use tax statutes cited above provide for an exemption from the general rule when contractors purchase building materials to be affixed to and made a structural part of real estate of a nonprofit hospital or nonprofit housing entity. (See Letter Ruling 79-13.) However, a contractor must pay use tax on property purchased by other tax-exempt entities and affixed by the contractor to the real estate of the purchasing entity, unless the tax-exempt entity paid the tax on the purchase of the property.

### Contractor/Retailers

A person engaged in the business of constructing, altering, repairing or improving real estate may also be engaged in the business of making sales at retail. For example, a contractor may make over-the-counter sales of building materials, or may, in the course of performing a construction contract, sell tangible personal property which will remain personalty rather than realty upon installation. Contractors who are also retailers are required to be licensed under the Sales Tax Act. Contractor/retailers holding a valid sales tax license are exempt from sales tax when purchasing tangible personal property for resale. When making such purchases, the licensed contractor/retailer must provide its sales tax license number to the supplier and include the phrase "for sale at retail" on the invoice or other sales document. (See Letter Ruling 89-63.)

A contractor/retailer will be exempt from tax when purchasing inventory for resale in the manner described above. However, the contractor/retailer will be taxed when material is removed from resale inventory in Michigan for the contractor/retailer's own use in a construction contract. The material is taxable in Michigan whether the contractor is using it in a construction contract in this state or elsewhere.

### Suppliers

Suppliers are persons in the business of selling building materials to contractors. Suppliers make sales at retail; contractors purchase property that will be affixed to and made a structural part of real estate in the performance of a construction contract.

Although the contractor is the consumer and must pay the sales or use tax due on the transaction, the supplier is liable for the collection and payment of the tax to the Department of Treasury. The supplier is relieved of this responsibility only when:

1. Building materials purchased by the contractor are to be affixed to and become a structural part of the real estate of a nonprofit hospital or nonprofit housing entity, or
2. Materials are purchased for resale.

The supplier must retain records of tax exempt sales to contractors. When the property is sold for resale, the supplier must retain sales documentation containing the contractor's sales tax license number and the phrase "for sale at retail." When the sale is of property to be affixed to a nonprofit hospital or nonprofit housing entity, the supplier must obtain the following exemption certificate. (See 1979 AC, R 205.71.)

### SALES OR USE TAX

Certification is made that the merchandise specified in the instrument to which this is made part will become part of the completed structure for a nonprofit hospital or a nonprofit housing entity qualified as exempt under the sales and use tax acts.

Should determination be made that any or all of this merchandise is used for a taxable purpose, it is agreed that tax, penalty, and interest will be paid to the seller.

Name of Exempt Entity \_\_\_\_\_

Name of Contractor \_\_\_\_\_

Signed By \_\_\_\_\_ Date \_\_\_\_\_