

New York State Department of Taxation and Finance
Office of Counsel
Advisory Opinion Unit

TSB-A-15(24)S
Sales Tax
May 29, 2015

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S120612A

The Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED] "Petitioner". Petitioner asks whether certain sales of equipment it makes and services it provides to its customers in New York State are subject to New York State and local sales tax. We conclude that Petitioner's installation of equipment constitutes a capital improvement and, therefore, its charges to its customers for the field equipment and the service of installing it are not subject to sales and use taxes.

Facts

Petitioner specializes in supply chain management services and distribution of high-quality components, equipment and materials for the electrical and telecommunications industries. Petitioner procures, warehouses, and delivers various kinds of electrical, communications and data products, components, and related services for its New York State customers. Petitioner is a distributor, but on occasion acts in a role similar to a "prime contractor" in connection with certain capital improvements for property owners.

A property owner (Property Owner) seeks an electrical distribution system upgrade at its New York facility, which will include the furnishing and installation of electrical equipment to replace existing medium voltage switchgear assemblies in the switch house of that facility. Petitioner asserts this project will constitute a "capital improvement," because it involves an addition or alteration to real property that is intended to become a permanent part of the realty and that either substantially adds to the value of the real property or appreciably prolongs its useful life. Property Owner hires a property manager (Property Manager) to act as its agent in connection with this capital improvement.

Property Manager enters into a contract with Petitioner (in this instance acting like a prime contractor) to provide all materials and labor necessary to replace the switchgear equipment at Property Owner's New York State facility. Switchgear equipment is the combination of electrical disconnect switches, fuses or circuit breakers that are used to control, protect and isolate electrical equipment. The switchgear appears as a metal enclosure that houses the main power to the building. There are conduits with cable that feed this enclosure, plus cables that extend out into the building itself. The switchgear is affixed to the building and located in a separate, locked room. The switchgear is bolted or otherwise attached to the floor of the room. This equipment is hard wired into the building's electrical system and is not intended to be moved or used elsewhere.

The labor charges include not only electrical installation services, but also "field services" that include: on-site engineering and design drawings; preliminary site work and coordination; demolition of old switchgear; development of a temporary power plan; coordination meetings with Property Owner and utility companies; design review of final switchgear, control wiring, and relaying; and start-up. Start-up testing includes inspection of the gear and wiring to make sure all connections are made properly and testing of the meters and circuit breakers for proper operation to make sure no shipping damage has occurred.

Property Manager issues a purchase order to Petitioner for the cost of materials and related field services to complete the project. Property Manager, as agent for Property Owner, completes Form ST-124, *Certificate of Capital Improvement* and timely provides it to Petitioner, who is listed as the contractor on the certificate. Property Owner also completes Form ST-124 and timely provides it to Property Manager, who is listed as the contractor on the certificate.

Upon receipt of the purchase order from Property Manager, Petitioner contracts with an electrical subcontractor (Subcontractor) to provide all materials and field services called for in Property Manager's order in connection with the capital improvement on Property Owner's premises. Subcontractor intends to supply the equipment, perform the work, and bill Petitioner for both material and labor charges incurred.

Although Petitioner states that it receives the Form ST-124, Petitioner asks the following questions, including what happens if it is not successful in acquiring the Form ST-124 from Property Manager:

1. The charges for materials and field services are separately stated from each other on Petitioner's invoice to Property Manager and Petitioner timely accepts in good faith a completed Form ST-124 certificate from Property Manager. Must Petitioner collect sales tax on any portion of the invoice?
2. The charges for materials and field services are not separately stated on Petitioner's invoice to Property Manager, but Petitioner timely accepts in good faith a completed Form ST-124 certificate from Property Manager. As the contract is a "capital improvement," may Petitioner refrain from charging sales tax on this invoice, even though the invoice is billed as a lump sum amount?
3. The charges for materials and field services are separately stated on Petitioner's invoice to Property Manager. However, Petitioner is unsuccessful in acquiring a Form ST-124 certificate from Property Manager. Although the overall contract performed at Property Owner's facility is a "capital improvement," must Petitioner charge sales tax on the materials portion of the invoice?
4. The charges for materials and field services are separately stated on Petitioner's invoice to Property Manager. However, Petitioner is unsuccessful in acquiring a Form ST-124 certificate from Property Manager. Although the overall contract performed at Property Owner's facility is a "capital improvement," must Petitioner charge sales tax on the labor or field services component of the invoice?
5. Petitioner is unsuccessful in acquiring a Form ST-124 certificate from Property Manager and the invoice is for a lump sum amount with the field services not separately stated from the materials on the invoice. Although the overall contract performed at Property Owner's facility is a "capital improvement," must Petitioner collect sales tax on the entire invoice amount?

Analysis

New York State and local sales and use taxes are imposed on all sales of tangible personal property, unless otherwise exempt, and on certain enumerated services. *See* Tax Law §1105(a) and (c). If Petitioner sells tangible personal property that it installs and that remains tangible personal property after installation, Petitioner is selling tangible personal property at retail and the sales are taxable.

However, any charges by a contractor (including charges for labor and material) to a customer for adding to or improving real property by a capital improvement are not subject to tax. *See* 20 NYCRR § 541.5(b)(2). The charges to the customer for tangible personal property that becomes part of a capital

improvement are not subject to sales tax because the contractor is the retail purchaser of such property. *See* 20 NYCRR §541.5(b)(1). When Petitioner acts as a contractor in installing tangible personal property that becomes part of a capital improvement, its receipts for such tangible personal property will not be subject to sales tax because Petitioner would not be selling tangible personal property at retail. In those situations, Petitioner (or Subcontractor, as the case may be) must pay sales tax on its purchases of tangible personal property to be installed as part of a capital improvement.

Tax Law §1101(b)(9) defines “capital improvement” as:

(i) An addition or alteration to real property which:

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

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

(C) Is intended to become a permanent installation.

See also, 20 NYCRR § 527.7(a)(3).

In addition, 20 NYCRR § 527.7(b), provides:

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

Whether a particular installation constitutes a capital improvement depends on the circumstances of a particular product and its installation. *See* TSB-A-94(43)S. Here, the first factor in the definition of “capital improvement” is satisfied, because the installation of the electrical switchgear would add to the value of the real property.

Petitioner also states that the switchgear assemblies will become a permanent part of the switch house. Removal would cause material damage to the real property and to the capital improvement affixed to it and is intended to become a permanent installation. The switch gear assemblies are bolted and otherwise affixed to the floor of the switch house and are hard wired to the premises. Petitioner notes that the switch gear is not intended to be moved or used elsewhere and is vital to the premises as it is directly linked to the building’s electricity supply. Petitioner further notes that if the switch gear were removed, doing so would remove power, lights, alarms, cooling and heat to the premises, which would cause damage to the premises (for instance, loss of power to the sump pump would cause water damage).

Accordingly, based on the information provided by Petitioner, we conclude that the installation of the switch house assemblies would qualify as a capital improvement to the real property for purposes of sales and use taxes under Articles 28 and 29 of the Tax Law. Although some elements of Petitioner’s charges for “field services” would not by themselves constitute capital improvements (e.g., demolition of old switchgear), these services nevertheless qualify as a capital improvement, whether or not the charges for these services are separately stated, because they are necessary elements of a construction project that results in a capital improvement. The charges for the installed materials and field services therefore would be exempt, whether or not they are separately stated on the invoice (Questions 1 and 2).

Petitioner's acceptance of Form ST-124 from Property Manager in good faith would relieve it from collecting any sales tax on the transaction.

With respect to Questions 3 through 5, 20 NYCRR § 541.5(b)(4) sets forth what happens if a certificate of capital improvement is or is not furnished to a contractor. The regulation provides:

(4) Documents; capital improvement contracts.

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

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

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

(ii) Where a contractor does not receive a capital improvement certificate from a customer, the contract or other records of the transaction will prevail. In such case:

(a) where the contractor does not receive a capital improvement certificate, collects tax on the full invoice price and the job is a capital improvement to real property, the contractor is liable for the tax on the cost of materials incorporated into the job, plus the tax collected from the customer. The customer is entitled to a refund of the tax paid to the contractor; or

(b) where the contractor does not receive a capital improvement certificate, collects no tax on the charges billed to the customer and the job is a capital improvement to real property, the contractor is liable for the tax on the cost of materials incorporated into the job performed.

(iii) If a contract includes the sale of tangible personal property which remains tangible personal property after installation, the contractor must collect the appropriate New York State and local taxes from the customer on the selling price, including any charge for installation, of the tangible personal property unless a properly completed exemption certificate is issued by the customer. The contractor may apply for a credit or refund of taxes he has paid on purchases of the tangible personal property that remain tangible personal property after installation.

The mere failure by Petitioner to obtain a properly executed ST-124 from its customer does not change the exempt nature of a capital improvement. While receipt of Form ST-124 in good faith relieves Petitioner from the obligation to collect sales tax on the transaction, failure to obtain this form places the burden on Petitioner to prove that the transaction was a capital improvement.

DATED: May 29, 2015

/S/

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NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion. The information provided in this document does not cover every situation and is not intended to replace the law or change its meaning.