

DEPARTMENT OF STATE REVENUE

Revenue Ruling #2016-03ST
May 3, 2018

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ISSUES

Sales and Use Tax - Tangible Personal Property Converted into Real Property

Authority: [IC 6-2.5-1-5](#); [IC 6-2.5-1-11.5](#); [IC 6-2.5-1-14.7](#); [IC 6-2.5-1-14.9](#); [IC 6-2.5-1-27](#); [IC 6-2.5-1-27.7](#); [IC 6-2.5-2-1](#); [IC 6-2.5-2-2](#); [IC 6-2.5-3-2](#); [IC 6-2.5-4-1](#); [IC 6-2.5-4-9](#); [45 IAC 2.2-4-1](#); [45 IAC 2.2-4-2](#); Sales Tax Information Bulletin #60 (November 2017).

A taxpayer ("Company") seeks a ruling regarding the following issues pertaining to its business:

1. Whether signage bolted to a foundation should retain its character as "tangible personal property" and signage embedded in the ground should constitute "real property" for Indiana sales & use tax purposes?
2. What are the Indiana state and local sales and use tax consequences of the sale, installation and repair of the signage that qualifies as tangible personal property to Company and its customers?
3. What are the Indiana state and local sales and use tax consequences of the sale, installation and repair of signage that qualifies as real estate to Company and its customers?

STATEMENT OF FACTS

Company is an out-of-state corporation that is in the business of designing, making, installing, and servicing custom signs. Company provides the following information regarding its business:

When a customer need[s] a sign, [Company's] representative surveys the installation site and determines what type of sign is needed. [Company] has artists that design the sign, once the customer accepts the proposal, [Company] makes the sign from raw materials at its facility either in Canada or in South Carolina, USA. Materials used in the production of signs include, but are not limited to, plastic, aluminum, steel, lamps, ballasts, transformers, neon, paint, bolts, screws, and vinyl. [Company] sells and install[s] different types of signage:

- (1) Towers;
- (2) Pylons;
- (3) Wall Signs;
- (4) Interior signs;
- (5) Menu board;
- (6) Directional sign;
- (7) Neon border tubing.

There are various methods of installation depending on the type of signs. All of the signs made by [Company] are installed by sub-contractor[s]. No signs are sold to any other contractor, fabricator, wholesaler, or retailer. [Company] does not keep an inventory of completed product, because every sign is custom designed and produced.

Company operates under time and material contracts. Company's charges include: a charge for the sign itself; a charge for installation; a charge for freight; a charge for a survey, if one is needed; an "engineering stamp fee," which is a professional, pass-through fee that may be required from the local government to secure a permit; and a fee for a permit that the local government may require to erect a sign. The customer is billed by Company. The customer does not make a separate payment to the subcontractor installer.

Company also repairs and performs other services to signs. This may include: repairs to broken or damaged parts; replacement of burned-out bulbs; neon repair; ballasts or transformer replacements; cleaning/washing; and painting. Company provides the labor and parts necessary to repair the sign and bills the customer accordingly.

Company makes, installs, and services many different types of signs using various installation methods. Company provides that the most common types of signs and methods of installation are as follows:

1. Towers: [S]tandalone structures that are not attached to buildings. Towers are bolted into foundations and may be removed without being damaged or damaging the real estate into which they are bolted.
2. Advertising pylons: [F]ree standing structures that may be bolted into . . . foundations or embedded or cemented into the ground. In the latter instance, the pylons may not be removed from the real estate without being damaged.
3. Wall sign: A business sign attached parallel to the wall of a building. This definition includes painted, individual letter, and cabinet signs located on the outside of a building, whether located on a wall, mansard, awning, canopy, or window. These signs are mounted by means of screws and bolts, and removal would result in varying degrees of damage to the building fascia. Additionally, individual letters may be mounted on a raceway that is used to reduce the damage to building fascia, but may result in some damage.
4. Neon border tubing: This is used to accent and illuminate building fascia and is attach[ed] by means of bolts and screws around the perimeter of a building.
5. Interior signs: Some examples of these are . . . interior signs which mount on the walls showing product brand names, wall plaques, etc. [These] signs can be mounted with bolts and screws or with adhesive tape. Damage might or might not occur to the wall upon removal of the sign.
6. Menu board: A sign associated with drive through windows and oriented toward drive through window traffic. The usual installation method is to install the sign in concrete base, although they are sometimes installed using anchor bolt method.
7. Neon border tubing: This is used to accent and illuminate building fascia and is attached by means of bolts and screws around the perimeter of a building.

DISCUSSION

Based on the foregoing facts, Company requests a ruling as to whether it is installing items that become incorporated into real property, and what the sales tax treatment would be regarding these transactions.

Pursuant to [IC 6-2.5-2-1\(a\)](#) and [IC 6-2.5-2-2\(a\)](#), sales tax is imposed on retail transactions made in Indiana. A retail transaction is defined in [IC 6-2.5-4-1\(b\)](#) as the transfer, in the ordinary course of business, of tangible personal property for consideration. [IC 6-2.5-4-1\(c\)](#) goes on to provide in pertinent part:

For purposes of determining what constitutes selling at retail, it does not matter whether:

- . . .
- (2) the property is transferred alone or in conjunction with other property or services . . .

"Tangible personal property" is defined in [IC 6-2.5-1-27](#) as:

. . . personal property that:

- (1) can be seen, weighed, measured, felt, or touched; or
- (2) is in any other manner perceptible to the senses.

The term includes electricity, water, gas, steam, and prewritten computer software.

A contractors' sales and use tax responsibilities with respect to the purchase, use, and sale of construction material are found in subsection (c) of [IC 6-2.5-3-2](#), which provides the following:

(c) The use tax is imposed on a contractor's conversion of construction material into real property if that construction material was purchased by the contractor. However, the use tax does not apply to conversions of construction material described in this subsection, if:

- (1) the state gross retail or use tax has been previously imposed on the contractor's acquisition or use of that construction material;
- (2) the person for whom the construction material is being converted could have purchased the material exempt from the state gross retail and use taxes, as evidenced by a properly issued exemption certificate, if that person had directly purchased the construction material from a retail merchant in a retail transaction; or
- (3) the conversion of the construction material into real property is governed by a time and material contract as described in [IC 6-2.5-4-9\(b\)](#).

[IC 6-2.5-4-9](#) further deals with a contractor's sales and use tax liability in construction contracts as follows:

- (a) A person is a retail merchant making a retail transaction when the person sells tangible personal property which:
- (1) is to be added to a structure or facility by the purchaser; and
 - (2) after its addition to the structure or facility, would become a part of the real estate on which the structure or facility is located.
- (b) A contractor is a retail merchant making a retail transaction when the contractor:
- (1) disposes of tangible personal property; or
 - (2) converts tangible personal property into real property;
- under a time and material contract. As such a retail merchant, a contractor described in this subsection shall collect, as an agent of the state, the state gross retail tax on the resale of the construction material and remit the state gross retail tax as provided in this article.
- (c) Notwithstanding subsections (a) and (b), a transaction described in subsection (a) or (b) is not a retail transaction, if the ultimate purchaser or recipient of the property to be added to the structure or facility would be exempt from the state gross retail and use taxes if that purchaser or recipient had directly purchased the property from the supplier for addition to the structure or facility.

"Construction material" is defined in [IC 6-2.5-1-14.7](#) as "any tangible personal property to be converted into real property." [IC 6-2.5-1-14.9](#) defines "Contractor" as "any person engaged in converting construction material into real property on behalf of another person. The term includes, but is not limited to, general or prime contractors, subcontractors, and specialty contractors." Finally, "time and material contract" is defined by statute at [IC 6-2.5-1-27.7](#) to mean "a contract in which the cost of construction material and the cost of labor or other charges are stated separately."

There is a difference in the tax collection and remittance requirements for construction material purchased by a contractor, which depends on whether the contractor is operating under a time and material contract or non-time and material contract (i.e., a lump sum contract). The Department's guidance on the topic is found in Sales Tax Information Bulletin #60 (November 2017). In interpreting [IC 6-2.5-3-2\(c\)](#), the Bulletin provides that when operating under a lump sum contract, contractors "purchase construction material for their own use or consumption in the fulfillment of contractual obligations to provide real property improvement services." Therefore, when a contractor operates this way, they "purchase construction material for their own use or consumption in the fulfillment of contractual obligations to provide real property improvement services." *Id.* A lump sum contractor's tax obligations would be the following:

- (1) pay sales tax at the time the construction material is purchased; or
- (2) self-assess and remit use tax at the time the construction material is converted into real property if that construction material was purchased or otherwise acquired without paying tax.

On the other hand, in interpreting the [IC 6-2.5-4-9\(b\)](#), Sales Tax Information Bulletin #60 provides that "contractors are retail merchants selling construction material when they (1) dispose of, or (2) convert construction material into real property under a time and material contract." *Id.* Due to sales of tangible personal property being subject to sales tax, which includes construction materials, "contractors converting construction material into real property under a time and material contract must collect and remit sales tax on the material portion of their contracts." *Id.*

"Installation charges" are specifically excluded from the definition from "gross retail income" per [IC 6-2.5-1-5\(b\)\(6\)](#) if they are "separately stated on the invoice, bill of sale, or similar document given to the purchaser." [IC 6-2.5-4-1\(e\)](#) provides additional guidance on charges for installation versus similar charges:

The gross retail income received from selling at retail is only taxable under this article to the extent that the income represents:

- (1) the price of the property transferred, without the rendition of any service; and
- (2) except as provided in subsection (g), any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records.

For purposes of this subsection, a transfer is considered to have occurred after delivery of the property to the purchaser.

Additionally, "the cost of materials used, labor or service cost, interest, losses, all costs of transportation to the seller, all taxes imposed on the seller, and any other expense of the seller" and "charges by the seller for any services necessary to complete the sale, other than delivery and installation charges" are included within the

definition of gross retail income which would be subject to sales tax in a retail sale. [IC 6-2.5-1-5\(a\)\(2\)](#) & (3). Further, "delivery charges" would also be considered part of gross retail income. [IC 6-2.5-1-5\(a\)\(4\)](#). "Delivery charges" are defined in [IC 6-2.5-1-5\(a\)](#) as follows:

. . . charges by the seller for preparation and delivery of the property to a location designated by the purchaser of property, including but not limited to transportation, shipping, postage charges that are not separately stated on the invoice, bill of sale, or similar document, handling, crating, and packing. Delivery charges do not include postage charges that are separately stated on the invoice, bill of sale, or similar document.

Turning to the first issue regarding the treatment of the signage as tangible personal property or not, Sales Tax Information Bulletin #60 provides additional guidance as to how the Department determines whether or not items remain tangible personal property:

"Construction Material" means any tangible personal property to be converted into real property.

1. Examples of construction material that may be converted into real property through incorporation or installation include, but are not limited to, doors, garage doors, windows, cabinets, garbage disposals, water heaters, water softeners, alarms, furnaces, central air conditioning units, gutters, carpeting and other flooring materials, drywall, lumber, asphalt, concrete, fencing, trees, shrubbery, and pre-fabricated construction material.
2. Examples of items that typically remain tangible personal property, and, therefore, *are not* considered construction material, include, but are not limited to, personal computers, televisions, refrigerators, stoves, dishwashers, clothes washers and dryers, window air conditioning units, and other removable items such as furniture.
3. Construction material that has been converted into real property when it has been attached to or incorporated into real property in such a way that would lead one to reasonably believe the construction material has been permanently affixed to the real property. Construction material incorporated into real property becomes part of and indistinguishable from the real property into which it has been incorporated.
4. Conversions of tangible personal property into real property include incorporations and installations of tangible personal property into facilities or structures. Incorporations and installations of tangible personal property into facilities or structures may include improvements to and repairs of existing facilities or structures.

Signage that is embedded in the ground would constitute construction material that has been converted into "real property" because one would reasonably believe the sign has been permanently affixed to the real property. Further, signs that are bolted or screwed to a foundation or building would be considered permanently affixed as well. Even if the bolts or screws could be removed without damaging the real estate or the sign, similar construction material such as water softeners and air conditioning units, which are often affixed in the same manner, are still considered by the Department to be part of the real property. Therefore, the signs that are bolted or screwed to a foundation or building would be considered incorporated into real property as well, as one would reasonably believe these signs have been permanently affixed to real property. Of the installation methods mentioned by Company above, only if the sign is affixed with tape would the signs remain tangible personal property.

In answer to the second and third questions, the consequences of the sale of signage that qualifies as either tangible personal property or real estate, it must first be clarified that in Company's situation, the signs (except for those affixed with tape) would be considered construction material when they are sold. The signs are construction material because they are not yet incorporated into real property when they are delivered to their customers in Indiana. The signs are only converted into real property after the subcontractors install them. [IC 6-2.5-13-1\(d\)\(2\)](#) provides that when a product sold to a customer "is not received by the purchaser at a business location of the seller," then "the sale is sourced to the location where receipt by the purchaser . . . occurs, including the location indicated by instructions for delivery to the purchaser (or donee), known to the seller." The sale would therefore be sourced to Indiana and be subject to Indiana sales tax.

Because Company operates using time and material contracts, Company is a retail merchant and must collect sales tax on the materials portion of the contracts. [IC 6-2.5-4-9\(b\)](#). Company's installation charges are separately stated on their invoices, so these charges would not be subject to sales tax per [IC 6-2.5-1-5\(b\)\(6\)](#), which provides that these type of charges are not included within gross retail income when separately stated. On the other hand, the freight charge would be subject to sales tax as a delivery charge because it constitutes a charge for transportation. [IC 6-2.5-1-5\(a\)](#). The charge for a survey, a permit, and the charge for an engineering stamp would all be taxable as gross retail income as well, as service costs or expenses of the seller. [IC 6-2.5-1-5\(a\)\(2\)](#).

Further, even though the signs that are installed using adhesive tape are not considered construction material because they are not converted into real property, the signs are still tangible personal property and would be subject to sales tax as a retail transaction pursuant to [IC 6-2.5-4-1](#).

As for any repair work, repair charges are typically exempt as a charge for a service. However, if the property being repaired is real property, then the tax treatment would depend on whether the repairs are performed pursuant to a lump sum contract or a time and materials contract. Separately stated repair parts in a time and materials contract would be subject to sales tax. If the repair parts are not separately stated and the true object of the transaction was the service, the cost of the parts would have to be ten percent or less of the cost of the service for the unitary charge to be exempt from sales tax, and Company would be required to pay sales or use tax on the parts. If the cost of the parts is more than ten percent, or the true object of the transaction was *not* a service, then the whole unitary charge is subject to sales tax. (See [IC 6-2.5-1-11.5](#); [45 IAC 2.2-4-1](#) and -2). Regarding charges for the services of cleaning, washing, or painting, this same "ten percent test" would apply if the charges for service and materials are not separately stated.

RULING

Company's signs are (with one exception) construction material that are converted into real property. Company is a retail merchant and must collect sales tax on the portion of the materials converted into real property and other charges that constitute gross retail income. Company must collect sales tax on the sign that is not converted into real property as well.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances as stated herein are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling a change in statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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