

**TENNESSEE DEPARTMENT OF REVENUE  
LETTER RULING # 06-21**

**WARNING**

**Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.**

**SUBJECT**

Application of sales and use tax to appliance sales by a natural gas utility district.

**SCOPE**

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the department by the taxpayer. The rulings herein are binding upon the department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling and a retroactive revocation of the ruling must inure to his detriment.

## **FACTS**

[TAXPAYER] is a political subdivision of the state of Tennessee, organized under the provisions of Tenn. Code Ann. § 7-82-101 *et seq.*<sup>1</sup>

The taxpayer sells, services and installs the following gas fired equipment: (a) heating and air conditioning systems, (b) floor furnaces, (c) water heaters, (d) logs, (e) fireplaces, (f) space heaters, (g) dryers, (h) ranges, (i) cooktops, (j) grills and (k) outdoor lights.

The taxpayer requires its customer to sign a contract and make a down payment before scheduling the work. The contract document states the equipment to be installed, labor to install and sales tax. The customer is billed at the time the installation is complete.

[LANGUAGE DELETED].

## **QUESTIONS**

1. Is the taxpayer the consumer of installed tangible personal property that becomes realty upon installation and therefore exempt from sales or use tax?
2. Is the taxpayer's sale of tangible personal property taxable?
3. The taxpayer requests guidance in determining taxation of the items lettered (a) through (k) above, including those which become real property and those which remain tangible personal property when installed.
4. Are taxpayer's service calls subject to tax?
5. What is the state tax rate on signed, uncompleted contracts as of July 15, 2002?
6. What are the procedures for obtaining a refund, including statutes of limitations, if tax has been paid on nontaxable sales?

## **RULINGS**

1. The taxpayer is the user and consumer of any tangible personal property that it installs if the property becomes a part of the realty upon installation. In this case, the taxpayer's exempt status would cause such property to be exempt from the sales or use tax.

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<sup>1</sup> The ruling request uses a cite to an earlier edition of the code, Tenn. Code Ann. § 6-2601. The present numbering is as given in the body of this ruling.

2. The taxpayer owes sales tax on the sale of tangible personal property to its customers, including installed tangible personal property that does not become a part of the realty upon installation.
3. The Department declines to rule on this question. However, guidance is given in the “Analysis” section that follows.
4. Service calls made in connection with the repair of real property are not subject to tax. Service calls where repair of tangible personal property is performed or contemplated are subject to tax.
5. In accordance with the ruling to Question 1 above, no tax is due with respect to tangible personal property that becomes a part of the realty upon installation. If the contract is for the sale of tangible personal property, including installed tangible personal property that does not become a part of the realty upon installation, the tax is due as of the date of sale. A sale occurs on the date that title, possession, or both passes to the customer. It would appear that title or possession would not have passed before July 15, 2002 on those contracts described as “uncompleted,” therefore, the state tax rate of seven percent (7%) would apply. If there is a sale of a single article of tangible personal property with a sale price greater than \$1,600.00, an additional state tax of two and three-quarters percent (2.75%) is due on the portion of the sale price between \$1,600.01 and \$3,200.00.
6. Refunds are governed by Tenn. Code Ann. § 67-1-1802. The statute of limitations provides that a refund claim must be filed on or before December 31 of the third calendar year following the date of the erroneous tax payment. The Department will refund tax collected from the taxpayer’s customers only if the taxpayer has credited or refunded such tax to its customers.

### ANALYSIS

1. The taxpayer is the user and consumer of any tangible personal property that becomes realty upon installation, but the taxpayer’s exempt status would cause such property to be exempt from the sales or use tax.

It has long been established that persons who erect or apply tangible personal property that becomes a part of realty are not making a “sale” for sales and use tax purposes; rather, such person is the user and consumer of such property. *Townsend Electric Co. v. Evans*, 193 Tenn. 536, 246 S.W.2d 967 (1952). TENN. COMP. R. & REGS. 1320-5-1-.07 recognizes this and provides that, in general, persons improving real property, either their own real property or for others, are users and consumers and therefore must pay the sales or use tax on material for use in making such improvements.

When the taxpayer purchases tangible personal property that becomes realty upon installation, the taxpayer is the user and consumer of such property. As the user and consumer of the property, generally, the taxpayer would be liable for the sales and use

tax. However, there is an important exemption contained in Tenn. Code Ann. § 67-6-329(a)(13), which exempts “[a]ll sales made to the state of Tennessee or any county or municipality within the state[.]” Therefore, as a political subdivision of the state of Tennessee, organized under the provisions of Tenn. Code Ann. § 7-82-101 *et seq.*, the taxpayer is not subject to sales and use tax on the tangible personal property it purchases for its own use.

2. The taxpayer owes sales tax on the sale of tangible personal property to its customers, including installed tangible personal property that does not become a part of the realty upon installation.

In the case of sales of tangible personal property, including installed tangible personal property that does not become a part of the realty upon installation; the taxpayer is not the user and consumer. Tenn. Code Ann. § 67-6-202 generally imposes sales tax on all sales of tangible personal property (unless specifically exempted from the tax). The service of installation of tangible personal property that remains tangible personal property upon installation is a taxable service. Tenn. Code Ann. § 67-6-102(a)(32)(F)(vi). Tenn. Code Ann. § 67-6-501 imposes the tax on the dealer. “Dealer” generally means any person engaging in activities subject to the sales or use tax. Tenn. Code Ann. § 67-6-102(a)(11). “Person” includes governmental agencies, with particular mention of utility districts that sell property and services that are subject to sales tax.<sup>2</sup> Tenn. Code Ann. § 67-6-102(a)(28). As a utility district, the taxpayer is a dealer for the sales of all property and services. As a dealer, the taxpayer has the obligation to collect sales and use tax when it sells taxable property and services to its customers. The taxpayer’s exemption from other taxes does not shelter taxpayer from its collection obligations. It should be noted, however, that Tenn. Code Ann. § 67-6-502 provides that, insofar as possible, the tax is to be collected from the customer.

3. The taxpayer requests guidance in determining whether specified items become exempt from sales and use tax as real property or remain taxable tangible personal property after installation.

Whether tangible personal property that is installed remains tangible personal property after installation or becomes part of the realty must be determined on a case-by-case basis by applying the law of fixtures to the factual circumstances that exist. The primary test for distinguishing tangible personal property from fixtures is not so much the manner in which the property is affixed to the realty as it is the intention with which the property is connected with the realty. The Tennessee Supreme Court has stated the test as follows:

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<sup>2</sup> Tenn. Code Ann. § 7-82-105 states that “[s]o long as a district shall own any system, the property and revenue of such system shall be exempt from all state, county, and municipal taxation.” However, the definition of “person” in the sales tax statute was expanded to include utility districts and other governmental agencies in the same legislation that extended the sales tax to sales of energy fuels and water. Ch. 38, Public Acts of 1963. Therefore, it is clear that the intent of Ch. 38 of the Public Acts of 1963 was to subject a public utility’s sales of tangible personal property and services to the sales tax, as applicable. *See also* Atty. Gen. Op., October 28, 1966.

“In Tennessee only those chattels are fixtures which are so attached to the freehold that, from the intention of the parties and the use to which they are put, they are presumed to be permanently annexed, or a removal thereof would cause serious injury to the freehold. The usual test is said to be the intention with which a chattel is connected with realty. If it is intended to be removable at the pleasure of the owner, it is not a fixture.”

*Magnavox Consumer Electronics v. King*, 707 S.W.2d 504, 507 (Tenn. 1986)(quoting *Hickman v. Booth*, 173 S.W. 438 (Tenn. 1914)).

Such intent may be shown by examining both objective and subjective factors. See *Hubbard v. Hardeman County Bank*, 868 S.W.2d 656, 660 (Tenn. Ct. App. 1993). Objective factors include the type of structure, the mode of attachment, and the use and purpose of the property. *Harry J. Whelchel Company v. King*, 610 S.W.2d 710, 713-714 (Tenn. 1980). The subjective factor is the expressed intent, if any, of the parties. See, *Id.* Tangible personal property becomes a part of the realty, though, if removing it would seriously damage the building to which it is affixed. *Process Systems, Inc. v. Huddleston*, 1996 Tenn. App. LEXIS 695 (Tenn. Ct. App. October 25, 1996)(citing *Memphis Housing Authority v. Memphis Steam Laundry-Cleaners, Inc.*, 463 S.W.2d 677, 679 (Tenn. 1971)). Tangible personal property also becomes realty if removal would destroy its essential character as personalty. *Id.* (citing *Green v. Harper*, 700 S.W.2d 565, 567 (Tenn. Ct. App. 1985)).

Thus, whether the personal property at issue becomes part of the realty depends on the particular factual circumstances that exist. For example, the court in *General Carpet Contractors, Inc. v. Tidwell*, 511 S.W.2d 241 (Tenn. 1974), examined carpet which was laid using the tackless strip method and was therefore easily removable. The court found that the carpet became realty because the parties installed it with the intent that it remain in place for the length of its useful life. *Id.* at 243. In another case, the court found that removal of the conveyor system at issue would damage the building and destroy the essential character of the conveyor system. *Process Systems, Inc., supra*. Accordingly, the conveyor system was held to be an improvement to real property. *Id.*

The ruling request does not set forth the facts with respect to any individual installation of the property in question. Therefore, the Department is not in a position to rule on this question based on the facts as supplied.<sup>3</sup>

4. Service calls made in connection with the repair of real property are not subject to tax, but service calls where repair of tangible personal property is performed or contemplated are subject to tax.

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<sup>3</sup> The Department could possibly issue a ruling on detailed facts concerning a specific item of property that is installed, i.e., “The taxpayer will install a [item] at the property of John Doe located at 123 Main Street, Anytown, Tennessee. The item is attached by means of [description]. John Doe owns the property which is his personal residence.”

The repair of tangible personal property is a taxable service pursuant to Tenn. Code Ann. § 67-6-102(a)(32)(F)(iv). However, repair to real property is not among the taxable services listed in Tenn. Code Ann. § 67-6-102(a)(32)(F). A service is taxable only if: (1) it is included in the statute listing the taxable services *Ryder Truck Rental, Inc. v. Huddleston*, 1994 Tenn. App. LEXIS 444, or (2) if it is performed as part of the sale of tangible personal property. Tenn. Code Ann. § 67-6-102(a)(32).

TENN. COMP. R. & REGS.1320-5-1.54 provides guidance on repair services, stating in pertinent part:

(1) All charges for repair services and repairs of any kind of tangible personal property, such as automobiles, clothing, watches and jewelry, office equipment, machinery, tires, etc., including all parts and/or labor, are subject to the Sales Tax. **This includes occasions when there may be no new parts involved in the transaction**, and occasions when a customer may furnish any or all of the parts necessary for the repair work. Any factor entering into the consideration charged for repair services and repairs such as **"service call,"** minimum charge, hourly or flat rates, mileage, etc., shall be subject to the Sales Tax.

(2) For the purposes of this rule, "repair services" and "repairs" of tangible personal property shall mean and include any one or all of the following for a user and consumer; ... **"service calls" where any repair work is done or contemplated;** ... Repair services and repairs of tangible personal property **shall not include any maintenance or other work on ... fixtures attached to and a part of any real property;** ... **service calls where no repair is contemplated;** . . . In the event any services and repairs are not taxable, the charges therefor must be billed separately to the customer and indicated as such on the books and records of the dealer.

(Emphasis supplied.) From the foregoing, it is clear that a service call for the purpose of making a repair to tangible personal property is subject to tax. Likewise, it is clear that a service call involving real property, or a service call where no repair is done or contemplated, is not subject to tax. The charges for such nontaxable services and repairs, however, must be billed separately to the customer and reported separately on the taxpayer's books.

5. It would appear that title or possession would not have passed before July 15, 2002 on those contracts described as "uncompleted," therefore, a sale would not have occurred and the state tax rate of seven percent (7%) would apply.

Effective July 15, 2002, the general state sales tax rate was raised from six percent (6%) to seven percent (7%). At the same time, a state tax at the rate of an additional two and

three-quarters percent (2.75%) was enacted applicable to the portion of the sale price of a single article falling between \$1,600.01 and \$3,200.00. Ch. 856, Pub. Acts 2002, codified at Tenn. Code Ann. § 67-6-202.

Ch. 856 of the Public Acts of 2002 also contained provisions for relief of taxpayers who had entered into fixed price or lump sum contracts for the improvement of real property on or before the effective date of July 15, 2002. However, as explained above, the taxpayer incurs no tax liability on contracts involving items that become part of the realty.

With respect to contracts involving items that remain tangible personal property upon installation, Ch. 856 of the Public Acts of 2002 contains no provision for relief. Dealers must collect sales tax on retail sales “at the rate provided by law of the retail sales price, as of the **moment of sale**[.]” Tenn. Code Ann. § 67-6-501(c) (emphasis added).

A “sale” of tangible personal property is defined by statute as “any transfer of title or possession, or both[.]” Tenn. Code Ann. § 67-6-102(a)(34)(A). Therefore, the rate in effect when either title or possession passes to the customer is the proper rate. For a contract for sale of tangible personal property not completed prior to the date of the tax rate increase, the higher rate, as well as the additional tax on a single article, applies. *Accord*, Atty. Gen. Op. 02-087, August 20, 2002.

#### **6. Refunds are governed by Tenn. Code Ann. § 67-1-1802.**

In the event the taxpayer has remitted tax paid to the Department in error, refunds are controlled by Tenn. Code Ann. § 67-1-1802 which reads in part:

(a) (1) The commissioner of revenue, with the approval of the attorney general and reporter, .... is empowered and directed to refund to taxpayers all taxes collected or administered by the commissioner that are, on the date of payment, paid in error or paid against any statute, rule, regulation or clause of the constitution of this state or of the United States. .... The authority granted in this subdivision (a)(1) extends only to taxes for which a claim is filed, with the commissioner under oath and supported by proper proof, within three (3) years from December 31 of the year in which the payment was made. .... Sales or use taxes which were collected from or passed on to customers by the taxpayer shall not be refunded unless the taxpayer has refunded or credited the sales or use tax to its customers.

If the taxpayer has remitted tax in error, it must file a refund claim with the Department, under oath and supported by proper proof, no later than December 31 of the third calendar year following the year in which the tax was paid. If the refund is for tax that has been collected from customers, the “proper proof” must include evidence that the tax has been refunded or credited to the customers.

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