



Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873

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Joint Committee on Finance

Paper #325

Sales and Use Tax Exemption for Modular and Manufactured Homes Used in Real Property Construction Activities Outside the State (General Fund Taxes -- Sales and Excise Taxes)

[LFB 2011-13 Budget Summary: Page 195, #2]

CURRENT LAW

Wisconsin imposes a 5% general sales and use tax on the sales price or purchase price of taxable items and services sold in this state. Sales of tangible personal property are generally subject to the tax, unless specifically exempted; whereas sales of services are generally exempt, unless specifically enumerated as a taxable service. Current law provides the following exemptions and exclusions from the tax for modular homes and manufactured homes: (a) purchase of a used manufactured home for use as a residency; (b) the sales price from the rental for a continuous period of one month or more of a manufactured home that is used as a residence; (c) 35% of the sales price for new manufactured homes; and (d) 35% of the sales price of certain modular homes, or the sales price minus the cost of materials that became component parts of the building being sold. Modular homes and manufactured homes have the following statutory definitions:

"Modular home" means any structure or component thereof which is intended for use as a dwelling and is either: (a) of closed construction and fabricated or assembled on-site or off-site in manufacturing facilities for installation, connection, or assembly and installation, at the building site; or (b) a building of open construction which is made or assembled in manufacturing facilities away from the building site for installation, connection, or assembly and installation, on the building site and for which certification is sought by the manufacturer that the modular home is built in accordance with the Uniform Dwelling Code. According to the Department of Revenue (DOR), nearly all modular homes are used in real property construction activities.

"Manufactured home" means either: (a) a mobile home; or (b) a structure that is designed to be used as a dwelling, with or without a permanent foundation, that is certified by the federal Department of Housing and Urban Development as complying with federal standards. According to DOR, manufactured homes can either be used in real property construction

activities or may retain the characteristics of tangible personal property.

GOVERNOR

Create an exemption from the state sales and use tax for modular homes and manufactured homes that are used in real property construction activities outside the state. The proposal would become effective on the first day of the third month beginning after publication of the bill. Assuming an effective date of October 1, 2011, the administration estimates that the proposal would reduce sales tax revenue by \$195,000 in 2011-12 and by \$260,000 in 2012-13.

DISCUSSION POINTS

1. According to DOR, current law provides that if a Wisconsin manufacturer sells a modular or manufactured home in Wisconsin to a dealer, the tax treatment is determined based on whether the home will become a real property improvement, or if the home will be sold as tangible personal property. DOR reports that it is common practice for modular homes and manufactured homes to be sold first by a manufacturer to a dealer, and then from a dealer to the final consumer.

2. If the modular or manufactured home retains the characteristics of tangible personal property when installed and the home is sold to the dealer in Wisconsin, sales tax is imposed on the final sale from the dealer to the consumer under current law (the sale from the manufacturer to the dealer is considered a sale for resale and is not subject to the sales tax). If the modular or manufactured home is sold by the dealer to a consumer outside the state and retains its characteristics as tangible personal property when installed, the transaction is not subject to Wisconsin sales tax and may be subject to the sales tax laws of that state. The Governor's proposal would not change the current imposition of tax under this circumstance.

3. Under current law, if a modular or manufactured home is destined to become real property when installed, the sales tax is imposed on the sale from the manufacturer to the dealer, if the sale to the dealer takes place in this state. The subsequent sale from the dealer to the customer is considered a sale of real property, which is not subject to the tax. The Governor's proposal would affect certain transactions of this type if the home is sold and installed by a Wisconsin dealer to a consumer located in another state.

4. If a modular or manufactured home is to be used in real property construction and is sold and transferred from a Wisconsin manufacturer to a dealer in another state to be sold and installed outside of Wisconsin, the transaction is not subject to Wisconsin sales tax but may be subject to sales tax in the state where installed. As noted, if the same home is first sold and transferred to a dealer in Wisconsin and subsequently sold and installed for a customer in another state, sales tax is due on the transaction from the manufacturer to the dealer. Other states, similar to Wisconsin, provide a credit for the amount of tax paid to other states against the amount of sales tax due to that state. Therefore, if a Wisconsin dealer sold and installed a modular or manufactured home in another state, such as Iowa, the dealer can credit the amount of tax paid to Wisconsin from the amount of tax due to Iowa on the final sale of the modular or manufactured home installed in Iowa. Since Iowa (as well as all of the surrounding states) has a higher state sales tax rate than Wisconsin, the entire amount of sales tax paid to Wisconsin by the dealer can be credited against the amount of sales tax due in Iowa. Net tax liability in this transaction is the same as if Wisconsin did

not impose any sales tax, and the dealer was, instead, subject only to Iowa's sales tax laws.

5. The Department has discovered through audits that certain dealers located in Wisconsin making such sales to Iowa customers had not remitted sales tax that was due to Wisconsin and, instead, remitted the sales tax to Iowa. Following audits, the dealers owed sales tax to Wisconsin but could not claim a credit in Iowa for taxes paid to Wisconsin because the tax years related to those sales were closed in Iowa. The table below shows the number of years that surrounding states permit businesses to adjust tax returns:

<u>State</u>	<u>Statute of Limitations</u>
Illinois	Three years from the month or period in which the taxable gross receipts were received (assessments issued on January 1 or July 1).
Indiana	The later of three years from the date the return was filed, or the end of the calendar year containing the period for which the return was filed.
Iowa	Three years from the date the return was filed, but four years from the date the return was filed for periods beginning in 2000.
Michigan	The later of four years from the date the return was due or the date the return was filed.
Minnesota	The later of three and a half years from the date the return was due or the date the return was filed.
Wisconsin	Four years from the date the return was filed.

Source: Commerce Clearing House

As a result, for sales of modular and manufactured homes made by these Wisconsin dealers to consumers in Iowa, the net sales tax paid to both states was higher than if the dealers had properly remitted tax to Wisconsin, and then claimed a credit against the amount of tax paid to Iowa in the final sale. The Governor's proposal would exempt Wisconsin dealers from paying tax to Wisconsin and would prevent these dealers from paying additional tax in future audits due to the complex nature of interstate taxation of modular and manufactured homes that are used in real property construction.

6. It should be noted that current law does not create an instance in which double taxation would occur for the sale of a modular or manufactured home that is used in real property construction outside this state. The situation described above is an example of how a dealer could pay tax to Wisconsin without receiving a credit for the same amount against the sales tax due to Iowa; however, if taxes were properly reported and remitted in the two states, the net amount of tax paid by the dealer would be the same under current law as compared to the Governor's proposal. It could be argued that Wisconsin dealers of modular and manufactured homes should be expected to know the tax laws of states in which they are doing business and should not receive the proposed exemption.

7. The proposal would abdicate Wisconsin's first right to impose sales tax on property that is first sold in this state for use outside this state. If Wisconsin dealers of modular and manufactured homes were to properly remit the sales tax for homes that are to become a real property construction outside this state as required under current law, DOR estimates that such sales

generate approximately \$260,000 of sales tax revenue, annually. Under the Governor's proposal, that amount would, instead, be collected in the state in which the home would become a real property construction.

8. Wisconsin generally uses destination-based sourcing for purposes of determining where the location of a sale occurs. The state sales and use tax is imposed on the sale from manufacturer to a dealer in this state because the subsequent sale is determined to be a sale of real property, which is not subject to the tax, even though the modular or manufactured home is destined for use by the final consumer outside the state. If the subsequent sale were to have retained the characteristics of tangible personal property and were sold to a person outside this state, the transaction would not be subject to Wisconsin sales tax because the sale would be sourced to the final destination outside the state. It could be argued that the proposed exemption from the sales tax would be consistent with the concept of destination-based sourcing under current law.

9. Under current law, if a dealer purchases a modular or manufactured home that becomes a real property construction from a Wisconsin manufacturer and takes possession of the home in another state, no sales tax is due to Wisconsin. According to DOR, most taxpayers do not want the burden of claiming a refund from other states, and do not, in practice, seek a credit against the sales tax paid in other states as a result of a Wisconsin audit. It could be argued that the Governor's proposal would reduce complexity and administrative burden for dealers located in this state as compared to those located in another state, making the business climate friendlier for dealers of modular and manufactured homes to do business in this state.

10. It could also be argued that the sales and use tax laws for dealers of modular homes and manufactured homes are not more complex than administration of sales tax law in other industries. Permitting an exemption from the sales tax due to complexity could encourage members of other industries to argue that complying with state sales tax laws is overly burdensome. It is difficult to determine whether complying with sales and use tax law for dealers of modular and manufactured homes is significantly more burdensome than for other industries.

11. Under current law, certain items sold for use in other states are exempt from the state sales and use tax, such as aircraft, motor vehicles, and truck bodies, if sold to nonresidents in Wisconsin but used outside of the state. It could be argued that the proposed exemption is appropriate, as it would create a similar type of exemption for modular and manufactured homes that become a real property construction outside this state.

ALTERNATIVES

1. Approve the Governor's proposal.
2. Delete provision.

ALT 2	Change to Bill
GPR	Revenue \$455,000

Prepared by: Sean Moran