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September 11, 1979

ATTORNEY GENERAL OPINION NO. 79- 201

The Honorable E. Richard Brewster
Kansas House of Representatives
3rd Floor, State Capitol
Topeka, Kansas 66612

Re: Taxation--Kansas Retailers' Sales Tax--Tax Imposed

Synopsis: Subsection (q) of K.S.A. 1978 Supp. 79-3603 imposes sales tax on services to items which were once tangible personal property, but which have been incorporated into real estate. Pursuant to that subsection, sales tax must be collected on gross receipts received for the providing of building maintenance and janitorial services.

* * *

Dear Representative Brewster:

You request our opinion as to whether the Kansas Retailers' Sales Tax Act requires the collection of sales tax on gross receipts received for the providing of building maintenance and janitorial services.

Subsection (q) of K.S.A. 1978 Supp. 79-3603 imposes sales tax upon certain services relating to personal property and provides as follows:

> "[A] tax at the rate of three percent (3%) upon the gross receipts received for the service of repairing, servicing,

> altering or maintaining tangible personal property which when such services are rendered is not being held for sale in the regular course of business, and whether or not any tangible personal property is transferred in connection therewith. The tax imposed by this subsection shall be applicable to the services of repairing, servicing, altering or maintaining an item of tangible personal property which has been and is fastened to, connected with or built into real property;"

Interpreting this statutory provision, the Kansas Department of Revenue has issued a ruling which states that most services, including janitorial services and other services specifically enumerated therein, upon real property are subject to sales tax under subsection (q).[1] As an example of how the statute is to be applied, the ruling states that "the service of cleaning a floor is taxable because it constitutes the servicing or maintaining of tangible personal property (the flooring material) which has been fastened to, connected with, or built into real property." The validity of this ruling depends upon the construction to be given to the second sentence of subsection (q).

In our judgment, the legislative history of subsection (q) of K.S.A. 1978 Supp. 79-3603 supports the ruling issued by the Department of Revenue. The sales tax imposed upon labor services relating to personal property was formerly a part of subsection (p) of K.S.A. 79-3603, which provided, prior to amendment in 1977, as follows:

> "[A] tax at the rate of three percent (3%) upon the gross receipts received from the installation, maintenance, servicing and repairing of tangible personal property not held for sale in the regular course of business, whether or not any tangible personal property is transferred in conjunction therewith, except services rendered in installing property in connection with the original construction of a building or structure, which when installed will become a part of such building or structure."

[1]See Revenue Ruling 19-78-4, attached hereto for your convenience.

Subsection (p) was amended in 1977 (See L. 1977, ch. 337, § 2) after the Kansas Supreme Court ruled that it was unconstitutionally vague and ambiguous. See Kansas City Millright Co., Inc. v. Kalb, 221 Kan. 658 (1977). Former subsection (p) was divided into two subsections: (p), pertaining to construction-related labor services; and (q), labor services relating to personal property. In the process of enacting subsection (q) and amending subsection (p), the Senate Committee on Assessment and Taxation adopted a "Statement of Legislative History Re 1977 S.B. 49."[2] The following comment is made therein relating to subsection (q):

> "The last sentence of subsection (q) was intended as an addition to and not a limitation on the first part of the subsection. The intent was to make it clear that personal property becoming a part of real estate retains its character as personalty for purposes of repair, servicing, alteration or maintenance." (Emphasis added.)

In our judgment, this declaration of legislative intent justifies the liberal construction of subsection (q) adopted by the Department of Revenue. The legislative history makes it clear that the purpose of the last sentence of the subsection was to impose sales tax on services to items which were once tangible personal property, but which have been incorporated into real estate. It is, therefore, our conclusion that subsection (q) of K.S.A. 1978 Supp. 79-3603 must be construed as imposing sales tax on the gross receipts received for the providing of building maintenance and janitorial services.

Very truly yours,

ROBERT T. STEPHAN
Attorney General of Kansas

Terrence R. Hearshman
Assistant Attorney General

RTS:BJS:TRH:jm

[2]Adopted April 29, 1977, attached hereto for your reference.

RULING 19-78-4

SALES TAX -- TAXABILITY OF SERVICES RENDERED UPON REAL PROPERTY. THE SALES TAX IS IMPOSED UPON THE SERVICE OF REPAIRING, SERVICING, ALTERING, OR MAINTAINING REAL PROPERTY WHERE THE COMPONENTS OF SUCH REAL PROPERTY WERE PREVIOUSLY TANGIBLE PERSONAL PROPERTY.

Advice has been requested concerning the application of the Kansas sales tax to services rendered in connection with the maintenance, servicing, alteration, or repair of real property. K.S.A. 79-3603 (q) imposes a tax on the gross receipts received for repairing, servicing, altering, or maintaining tangible personal property whether or not it has been fastened to, connected with, or built into real property. Therefore, all maintenance, alteration, or repair services are taxable under K.S.A. 79-3603 (q), if rendered in connection with components of real property where the components were tangible personal property prior to being fastened to, connected with, or built into real property.

Most services performed upon real property are subject to the sales tax under the above section. For example, the service of cleaning a floor is taxable because it constitutes the servicing or maintaining of tangible personal property (the flooring material) which has been fastened to, connected with, or built into real property.

The following are further examples of the service of repairing, servicing, altering, or maintaining which would be subject to sales tax under K.S.A. 79-3603 (q):

window washing
tree trimming
janitorial services
welding
exterminator's services
sand blasting
snow removal
drain cleaning services
septic tank cleaning
painting
brick and fireplace cleaning
demolition
swimming pool cleaning

Statement of Legislative History Re 1977 S.B. 49
Adopted by
Senate Committee on Assessment and Taxation
April 29, 1977

Subsection (p) of Section 79-3603, as enacted in 1970, imposed a tax:

> ". . . upon the gross receipts received from the installation, maintenance, servicing and repairing of tangible personal property not held for sale in the regular course of business, whether or not any tangible personal property is transferred in conjunction therewith, except services rendered in installing property in connection with the original construction of a building or structure, which when installed will become a part of such building or structure."

In Kansas City Millwright Company, Inc., v Kalb, decided March 5, 1977, the Supreme Court upheld a district court decision which found the above subsection to be unconstitutionally vague. The Court cited inconsistencies in rulings by the Department of Revenue in interpreting the section, and noted three terms which cause particular concern to those liable for the collection of the tax - "tangible personal property," "original construction," and "structure".

"Tangible Personal Property". While agreeing with the reasonableness of an interpretation by the Department that the legislature did not intend to tax the maintenance, servicing and repairing of real property, the Court found problems in determining what is "tangible personal property," the maintenance, servicing and repairing of which is taxable, and what is real estate the maintenance, servicing and repairing of which is not taxable, and in determining what is the installation of tangible personal property and what is the maintenance, servicing and repairing of real estate.

S.B. 49 addresses these problems in two ways. First, subsection (p) is amended to impose a tax solely on the service of installing or applying tangible personal property whether or not such personal property remains personal property or becomes a part of real estate (except when such property is installed in connection with the original construction of a building or facility). This language would, for instance, clearly make taxable charges for labor services performed in re-painting (applying paint to) a building. Previously this had been ruled exempt as a repair to real estate, whereas labor performed in re-plumbing a building was held taxable as installation of tangible personnal property.

Secondly, there is added a new subsection (q), which imposes the tax on the service of repairing, servicing, altering or maintaining tangible personal property per se, and further makes the tax applicable to the services of repairing, servicing, altering or maintaining an item of tangible personal property which has been and is fastened to, connected with or built into real property. An alternative to the latter provision that was considered but rejected was inclusion of a lengthy list of articles for which services fo repairing, servicing, altering or maintaining would be taxable regardless of the extent of their connection with real property. The language adopted was felt to cover the same items without attempting to set out an all inclusive list from which any omission would be significant. The last sentence of subsection (q) was intended as an addition to and not a limitation on the first part of the subsection. The intent was to make it clear that personal property becoming

a part of real estate retains its character as personalty for purposes of repair, servicing, alteration or maintenance.

These revisions remove the basis for the earlier interpretation of legislative intent as being not to tax maintenance, servicing or repairing of real estate, since under them the tax on labor services would apply not only to work on fixtures but to work on any item of personal property that has become a part of real estate. For instance, labor services rendered in repairing roofing, siding, door frames, or other parts built into a house or other building would be taxable.

The revised language thus eliminates a distinction that contributed to inconsistent rulings. For instance, the Court's opinion noted rulings that repairs to a garage or to guttering were exempt as repairs to real property, but that replacing a garage door or installing new guttering were taxable as installations of tangible personal property. Under the language of S.B. 49, either type of service clearly would be taxable.

Another problem that S.B. 49 would solve is illustrated by a question and answer quoted in the Court's opinion. The question was whether the sales tax applies to service charges for the installation of augers, roller mills, electric motors and other machinery for handling grain when this equipment is installed at the time of new construction. The answer, in part, was that charges for installation of such property are not taxable if the tangible personal property is so affixed to the building or structure as to become a part thereof, and that the question of whether it is so affixed depends on the facts in each individual case. Under the language of S.B. 49, application of the tax is the same whether or not the personal property

installed becomes a part of real estate, and the exception for original construction does not depend on whether the property installed becomes a part of the building or facility.

The Court also was critical of the position of the Department that any interior remodeling of a building is taxable as it will always include the installation of tangible personal property, while there is no charge for roof alterations as this is repair to a building. Under S.B. 49, both would be taxable.

"Original Construction". The Court's opinion stressed the lack of any definition of original construction. For purpose of subsection (p), S.B. 49 defines "original construction" as including: (a) first or original construction of a building or facility; (b) the addition of an entire room or floor or completion of an unfinished part of an existing building or facility (as in the development of a shopping center, for instance, where a shell may be put up and partitions added as space is leased to different businesses); and (c) restoration, reconstruction, or replacement of a building or facility damaged or destroyed by specified disasters such as fire, flood, or storms. This "act of God" loss provision was suggested in part by a plea for elimination of the tax in the costly program of restoring Topeka's Grace Cathedral as a cultural and historic landmark after a fire which left only stone walls and towers standing. Services employed in replacement, remodeling, restoration, renovation or reconstruction under any circumstances other than those specified would be taxable. In Committee discussion, it specifically was noted that voluntary razing of an old building and erecting a new one on the same foundation

would not in itself, under the language of the subsection, qualify as new construction. These detailed provisions are designed to provide the clarity of meaning which the Court found lacking in the use of the words "original construction" alone.

The opinion noted rulings that the addition of an upper floor to an existing structure is considered to be original construction, but that reconstructing a tornado destroyed house on the original foundation would not be, and that complete remodeling to convert an office building to a manufacturing facility, retaining only the bare structure of the building, would not be considered to be original construction. Under S.B. 49, only one of these rulings - reconstruction of the tornado destroyed house - would be changed, and that by express language added as a matter of policy. The other two rulings would be the same, but would be based on express statutory language rather than on administrative determinations.

"Structure". The Court's opinion also was critical of the word "structure" as not having a well defined meaning in law or in usage by the Department of Revenue. S.B. 49 replaces the word "structure" with the word "facility," which is used and defined in the Job Expansion and Investment Credit Act of 1976, and which includes land improvements immediately surrounding the facility. The definition of "facility" in S.B. 49 is similar to that found in the above act but was expanded to include conveyance, transmission, or distribution lines of rural electric cooperatives, rural water districts, and municipal utilities, oil or gas wells and water wells, in addition to mills, plants, refineries, and feed lots. Inclusion of other transmissi

lines such as pipelines and telephone lines in the definition was considered but rejected.

A House Committee of the Whole amendment added language expressly stating that the tax does not apply to labor services in the construction, reconstruction, restoration, replacement or repair of a bridge or highway. (Bridges and highways previously had been considered to be structures, with labor services in original construction exempt.)

Portions of the above definition were added as a policy decision to try to preserve the status quo as to how the tax is being accounted for or not accounted for in actual practice. While the consistency of some of the decisions as to what should be included in the definition of a facility and what should not may be open to question, the definition does provide a statutory standard in another area found by the Court to need clarification.

While the Court decision does not mention the lack of a definition of "building," one is added by S.B. 49. The definition again is similar to one contained in the Job Expansion and Investment Credit Act, and includes enclosures within which individuals customarily live or are employed, or which customaril are used to house machinery, equipment or other property, and including land improvements immediately surrounding such building.

In summary, the revision of the prior subsection (p), including its division into two subsections and the addition of definitions of key terms, represents a legislative effort to correct the deficiencies found by the Court and thus to preserve sales tax revenues in an amount approximately equal to revenues collected under subparagraph (p) prior to the Court's decision.

As Introduced

1. Divided K.S.A. 1976 Supp. 79-3603(p) into two subsections: (p) pertaining to construction related labor services; and (q) labor services relating to personal property as such, i.e.; repairs to automobiles, appliances, etc.

2. Deleted from subsection (p) the words "or structure" in the exclusion from the tax of charges for services rendered in original construction.

3. Added in K.S.A. 1976 Supp. 79-3606 an exemption of prescribed drugs, insulin, and prescribed orthopedic and prosthetic appliances.

4. Defined "prosthetic and orthopedic appliances."

As Amended by Senate Committee

1. Added liquor gallonage tax increases intended to offset the revenue cost of the drug exemption.

2. Inserted the word "facility" in place of "structure", and defined facility to include a mill, plant, refinery, electrical transmission line, electrical distribution line or feed lot, and land improvements immediately surrounding such facility.

3. Defined the word "building."

4. Clarified the drug exemption, limiting it to prescription only drugs; and limited the appliance exemption to exclude motor vehicles, motor vehicle accessories, or fixtures to real property.

As Further Amended by Senate Committee*

1. Removed from the bill the gallonage tax increase. (The gallonage tax increase was introduced separately as S.B. 458, with CMB added and the rate on both beers adjusted downward.)

2. Revised subsection (p) of 79-3603 to make the tax applicable to services in installing or applying personal property whether or not it remains personal property or becomes a part of real estate.

3. Made the tax imposed by subsection (p) applicable only to services rendered after the effective date of the act and pursuant to a contract entered into after May 15, 1977.

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* Subsequent to handing down of opinion in Kansas City Millwright Company v. Kalb.

4. Defined "original construction" to include addition of an entire room or floor, completion of an unfinished portion of an existing building or facility, and restoration, reconstruction or replacement of a building or facility damaged or destroyed by fire, flood, storms or various kinds, explosion, or earthquake.

5. Expanded the definition of "facility" to include oil or gas wells or water wells.

6. Added a sentence to subsection (q) making the tax imposed by it applicable to charges for repairing, servicing, altering or maintaining an item of personal property which has been fastened to, connected with or built into real property.

7. Expanded the aircraft remanufacture and modification exemption in 79-3606 (g) to include labor services as well as parts.

8. Changed the effective date of the bill from publication in the statute book to publication in the official state paper.

As Amended by Senate Committee of the Whole

1. Amended the definition of "facility" in subsection (p) by deleting "electrical transmission line, electrical distribution line" and substituting any conveyance, transmission or distribution line of any rural electric cooperative, municipal utility, or rural water district.

2. Cleaned up the effective dates of amendments to 79-3603 (publication in state paper) and 79-3606 (July 1, 1977).

As Amended by House Committee

1. Defined "retailer" to include contractors, subcontractors or repairmen engaged in other than original construction, with conforming changes in other sections. (H.B. 2207 with some revision.)

2. Defined "municipal corporation" and "quasi-municipal corporation" as used in a Senate Committee of the Whole amendment to 79-3603(p).

3. Made alcohol and spirits, wines and strong beer subject to the 3 percent sales tax. (Intended to replace the liquor gallonage and CMB tax increases as an offset to the revenue cost of the sales tax drug exemption.)

As Amended by House Committee of the Whole

1. Removed the amendments by the House Committee defining "retailer" as including some contractors and making related changes. (H.B. 2207)

2. Added amendments relating to application of the sales tax to rentals of mobile homes.

3. Added in 79-3603(p) language excluding from the application of the tax charges for labor services in the construction, reconstruction, restoration, replacement or repair of bridges or highways.

4. Added in 79-3606 an exemption for purchases by groundwater management districts. (H.B. 2055)

5. Reworded language previously added to 79-3603(p) to exclude from the tax imposed by this subsection charges for services rendered on and after the effective date of the act pursuant to a written fixed price contract entered into prior to May 15, 1977.

6. Amended into the bill the provisions of previously passed H.B. 2360, which also had amended 79-3606 as it relates to contractor audit records.

As Amended by Conference Committee

1. Deleted the subsection imposing the sales tax on alcohol and spirits, wines and strong beer. (Gallonage and CMB rate increases similar to those in S.B. 458, and designed to offset the revenue cost of the drug exemption, were amended into H.B. 2396.)

2. Deleted the amendments relating to application of the sales tax to rentals of mobile homes.