Bartel

IN THE DISTRICT COURT OF LANCASTER COUNTY, NEBRASKA

HERITAGE HOMES OF NEBRASKA, INC., a Nebraska Corporation,	)	Docket 522 Page 297
Petitioner,	)	
v.	)	ORDER
DEPARTMENT OF REVENUE, and M. Berri Balka, Tax Commissioner,	)	
Respondents.	)	

Statement of the Case

Heritage Homes ("Heritage") appeals a decision of the Department of Revenue ("Department") and the State Tax Commissioner ("Commissioner") that denied a portion of a claim for a refund of Nebraska sale and use tax. The appeal has been filed pursuant to Neb. Rev. Stat. §§ 77-2708(2) (Supp. 1995), 77-27,127 (Reissue 1990) and 84-917 (Reissue 1994).

Heritage constructs modular homes and buildings and also attaches them to the realty the purchaser desires. In December of 1989, Heritage filed an election with the Department to be treated as an "Option 2" contractor for sales and use tax purposes. As an Option 2 contractor, Heritage agreed to be treated as a contractor maintaining a tax paid inventory.

Heritage filed a claim seeking a refund of $54,927.13 for sales and use tax paid on materials purchased and used in the construction of modular homes and buildings. These particular materials were used in homes and buildings that were built in

Nebraska and later attached to real estate outside of Nebraska. The Department granted a refund totalling only $17,524.26. This amount represented tax paid on materials which constituted tangible personal property purchased from out-of-state vendors that were not licensed to collect Nebraska taxes pursuant to the temporary storage exclusion provided for in §§ 77-2702.19 and 77-2703.23 (Cum. Supp. 1994). Heritage has filed this claim seeking a refund of the remaining $37,402.87.

Analysis

Heritage constructs modular homes and buildings and attaches them to the real estate. As such, Heritage is a "contractor" under Nebraska law. *See* Neb. Rev. Stat. § 77.2702.05 (Cum. Supp. 1994)("Contractor . . . shall mean any person who . . . annexes property to . . . real estate . . . ."). "A contractor . . . can elect to be treated in one of [two] ways for sales tax purposes: (1) as a retailer, [or] (2) as a consumer of property annexed to real estate who pays the sales tax or remits the use tax at the time of purchase and maintains a tax-paid inventory." *George Rose & Sons Sodding and Grading Co. v. Nebraska Department of Revenue*, 248 Neb. 92, 96, 532 N.W.2d 18, 22 (1995).

These two options are detailed in the Sales and Use Tax Regulations created by the Department. For example, regulation 1-017.05A, described as "OPTION 1", allows the contractor to elect "[t]o be treated as a retailer, with a tax free inventory. Under this option, the contractor is a retailer of those items that become a part of real estate . . . .". As a result, the contractor

can purchase building materials and not pay any tax at that time. However, the contractor has to collect a sales tax at the time of the sale of the modular unit. In contrast, under regulation 1-017.06 described as "OPTION 2", a contractor can elect "[t]o be treated as a contractor with a tax-paid inventory. Under this option the contractor must pay the sales or use tax on all building material when purchased or received." As a result, when an Option 2 contractor sells and annexes the property to the real estate, the contractor does not have to collect and remit sales tax.

Heritage elected to be an Option 2 contractor and pay taxes when it purchased the materials used in the construction of its modular units. There is no controversy regarding transactions where the modular units are annexed to property within Nebraska. However, the controversy arises when Heritage sells and annexes the modular units to real estate outside of Nebraska. For example, when Heritage annexes a unit to real estate in Iowa, Iowa has categorized Heritage as a retailer and required Heritage to pay sales tax. Iowa has also not allowed Heritage a credit for taxes Heritage has paid in Nebraska.

Contractors electing Option 1 and therefore not paying a tax when purchasing materials, can "withdraw[] from tax free inventory for annexation to real estate in another state, without a use tax liability being incurred by the contractor." Reg. 1-017.05C. Whereas, those contractors electing Option 2 receive "no Nebraska credit . . . on materials subject to the sales tax that are withdrawn from tax-paid inventory for annexation to real estate in

another state." Reg. 017.06A.

Heritage argues that they should be able to disregard their Option 2 status when they annex modular units to real estate outside of Nebraska. It is clear that Heritage may not be both an Option 1 contractor and an Option 2 contractor simultaneously because "[a] contractor may not operate under more than one option at the same time". Reg. 1.017-08A. Heritage alternatively suggests that they should be regarded as a "manufacturer" and not a contractor to avoid having to pay a Nebraska tax when they purchase the inventory and then pay an Iowa tax when they annex modular units to Iowa real estate. Heritage suggests that they cease to be a contractor and become a manufacturer in a particular case solely because the property in that given case is annexed to Iowa real estate and not Nebraska. This argument is similar to Heritage asking to operate under more than 1 option at one time. The fact is Heritage has made the business decision to operate as an Option 2 contractor which does not allow any kind of credit for personal property annexed to real property outside of Nebraska. *See supra* Reg. 1-017.06A. On the other hand, Option 1 does provide for a contractor to avoid having to pay a Nebraska tax and an Iowa tax. *See supra* Reg. 1-017.05C. The regulations adopted by the Department in this case have the effect of statutory law. *Nucor Steel v. Leuenberger*, 233 Neb. 863, 866, 448 N.W.2d 909, 911 (1989).

To tax Heritage in such a manner does not violate the Commerce Clause. As the United States Supreme Court has held, "the Commerce

Clause does not forbid the actual assessment of a succession of taxes by different States on distinct events as the same tangible object flows along." *Oklahoma Tax Commission v. Jefferson Lines, Inc.*, 115 S. Ct. 1331 (1995). Furthermore, "[t]he multiple taxation placed upon interstate commerce by such a confluence of taxes is not a structural evil that flows from either tax individually, but it is rather the 'accidental incident of interstate commerce being subject to two different taxing jurisdictions'". *Jefferson Lines* at 1342 (quoting in part from Lockhart, Gross Receipts Taxes on Interstate Transportation and Communication, 57 Harv. L. Rev. 40, 75 (1943)). As a result, taxing Heritage in such a manner does not violate the Commerce Clause.

Therefore, the decision of the Department and the Commissioner is affirmed.

Date: December 23, 1996.

BY THE COURT:

Donald E. Endacott

Donald E. Endacott
District Judge