

**M e m o r a n d u m****190.0256** □

To: Oakland – Audit (O. D. Millette)

Date: December 28, 1990

From: Donald J. Hennessy  
Senior Tax Counsel

Subject: Relocatable Classrooms

This is in reply to your memorandum to me of October 15, 1990. I am enclosing a copy of our proposed amendments to Regulation 1521, Construction Contractors, and 1660, Leases of Tangible Personal Property in General. The amendments deal with relocatable classrooms. While such amendments have not yet been heard by the Board, they have been discussed with industry and are being used in decision making in this difficult and constantly changing area. I recommend a thorough reading of such proposed regulations by any auditor who must presently audit a relocatable classroom manufacturer or dealer. You may want to give thought to delaying such audits until the amended regulations are adopted by the Board and OAL. The proposed regulations should be your primary source of answers to questions from the public.

The first specific question you raise in your memorandum is, “In what situations do we consider sales or leases of relocatable classrooms as of real property, not tangible personal property, and therefore, not subject to sales or use tax?” An auditor must remember that, unfortunately, we have four time periods, during each of which relocatable classroom transactions are taxed differently:

## (1) Pre-June, 1989

This was back in the quiet days before there was any Board or legislative activity on relocatable classrooms. For this period, the sale of a relocatable classroom was a sale of tangible personal property (Steel Guard, Inc. v. Jannsen 171 Cal.App.3d 79), with tax applying to the entire contract price, with the usual rules applying as to transportation charges, installation charges, and allocation of local tax.

## (2) June 19, 1989 to September 25, 1989

This is the period covered by the Board’s amendment to Regulation 1521(c)(3) (still in tax service) stating:

“A contract to furnish and install a relocatable classroom, or other prefabricated or modular building of similar size, is a construction contract whether the building rests in place by its own weight or is physically attached to realty. It is immaterial

whether the building is erected upon or affixed to land owned by the owner of the building or is leased to the landowner or lessee of the land.”

During such period sales tax did not apply to a contract to furnish and install a relocatable classroom. The installing contractor was the consumer of “materials” and the retailer of “fixtures” going into such relocatable classroom as set forth in Regulation 1521(b)(2).

(3) September 26, 1989 to September 12, 1990

This is the period covered by the original section 6012.6 (Stats 1989, Chapter 816, AB 1051). During this period, the sales tax applied to 40% of the selling price of a “factory-built school building” when furnished and installed for a school or school district. “Factory-built school building” was limited during this period to buildings capable of being occupied by pupils. It excluded buildings used exclusively for warehouse, storage, garage, or district administrative office purposes.

(4) September 13, 1990 and thereafter

This is the period covered by the amendments (Stats 90, Chapter 763, AB 4029) to section 6012.6, which broadened the coverage of the statute to include community college districts, and deleted the provision relating to possible liability of purchasers. Also, the definition of “factory-built school building” was liberalized so that administrative buildings, storage buildings, etc. would be included. Such definition would include all of the specialized buildings listed on Page 2 of your letter, provided they otherwise meet the definition of “factory-built school buildings”, i.e., special education units, restrooms, resource centers, remedial classes, libraries, book stores, student project/activity centers, computer rooms, factory offices, administrative offices, first-aid and weight rooms.

You will note in the proposed amendments to Regulation 1660, as a matter of interpretation, leases of factory-built school buildings are considered as leases of real property, with the lessor as the consumer. If the lessor is the manufacturer tax applies to cost; if the lessor is not the manufacturer tax applies to 40% of the selling price to such lessor.

Therefore, the answer to your first question as to real property is that from June 19, 1989 to September 25, 1989 the furnishing and installation of a relocatable classroom was a construction contract. In addition, all leases of relocatable classrooms on and after September 26, 1989 are leases of real property.

You will note that the proposed amendments to Regulation 1521 do not change subdivision (c)(3) which states that prefabricated units such as commercial coaches, house trailers, etc. registered with DMV or the Department of Housing are tangible personal property. Sales of such units, even though used as relocatable classrooms, are taxable at 100% of the

selling price. Such units simply do not satisfy section 6012.6's requirement of approval by the structural safety section of the Office of the State Architect.

Your memorandum next relates that your major problem is as to the size of relocatable classrooms, or buildings which are similar in size to, but are not, relocatable classrooms. You are correct that any building may be a "factory-built school building" if it satisfies section 6012.6. regardless of size. There are no maximum or minimum sizes for relocatable classrooms.

As to buildings which are not "factory-built school buildings", the proposed amendments to Regulation 1521 state"

"A contract to furnish and install a ~~relocatable classroom or other~~ prefabricated or modular building ~~of similar in size to~~, but which is not, a factory-built school building (relocatable classroom) is a construction contract whether the building rests in place by its own weight or is physically attached to realty. It is immaterial whether the building is erected upon or affixed to land owned by the owner of the building or is leased to the landowner or lessee of the land."

"Generally, a contract to furnish and install a small prefabricated building, such as a shed or kiosk, which is movable as a unit from its site of installation, is a construction contract only if the building is required to be physically attached to real property by the seller, upon a concrete foundation or otherwise. The sale of such a unit to rest in place by its own weight, whether upon the ground, a concrete slab, or sills or piers, is not a construction contract even though the seller may deliver the unit to its site of use."

Therefore, regardless of how small the building, e.g., shed or kiosk, if the contractor is required to attach it to real property (e.g., by pin, screw, bolt, or any other device), the contract is a construction contract, with the contractor the consumer of materials and retailer of fixtures. These provisions in amended Regulation 1521 will have a definite bias towards seeing most "buildings" as improvements to real property. We do not want to go back to the days of trying to argue that a three-story building is tangible personal property for sales and use tax purposes. Hopefully, by a process of elimination, Regulation 1521 should leave us with only unattached "sheds or kiosks" as a problem, as to which the regulation will say "is movable as a unit" if it is to be considered tangible personal property. In deciding whether a shed or kiosk is "movable as a unit" we should look to the ordinary practice of the industry. Almost anything is movable as a unit if you get a large enough crane. That is not the test.

We agree with your suggestion that we not identify what qualifies as relocatable classroom sizes, and then allow only identical size buildings as construction contracts. The test is similar in size, not identical. Therefore, the installation of some unattached buildings smaller than those qualified as relocatable classrooms may still be construction contracts, if they are similar in size. Uniformity here will require communication between auditors and a consistent audit review process.

As to the petition case you refer to, [X], "porta house" units consisting of numerous prefabricated wood panels are bolted together in a variety of configurations and sizes, any where from 9 to 24 feet wide, in any length, with doors and windows, with or without floors. No tax was paid on acquisition of the panels by [X]; your audit taxed all rental receipts as from a lease of tangible personal property regardless of size of the assembled leased unit.

Proposed Regulation 1660(d)(8) applies to [X]'s petition. These "porta house" units, after installation, are "structures" and should be treated as leases of real property. Tax applies as in Regulation 1521. We recommend a reaudit.

I am afraid I cannot simplify things further as you hoped. The taxation of sales of relocatable classrooms must depend on which of the above listed four time periods applies. Prefabricated or modular buildings of "similar" size will be considered construction contracts, but we still will have prefabricated units registered with DMV or the Department of Housing that will be tangible personal property.

A couple of additional points as to relocatable classrooms. Proposed Regulation 1521(c)(4)(B)(2) has caused confusion already as to who may issued resale certificates. We have interpreted such language to mean that a resale certificate may be issued if the purchaser is to resell without installation, but may not be given if the purchaser has an existing contract to furnish and install for a school district or community college district, the 40% measure applies on the purchaser's resale, the purchaser cannot consider itself the consumer in such situation and pay on 40% of its purchase price.

DJH:es