M e m o r a n d u m

275.0127

To: Mr. Glenn A. Bystrom
Principal Tax Auditor

Date: December 20, 1990

From: Ronald L. Dick
Senior Tax Counsel

Subject: Taxability of Compressed Natural Gas

This is in reply to your October 29, 1990 memorandum regarding the application of sales tax to charges for Compressed Natural Gas (CNG) when sold and delivered into vehicles through a delivery system connected to a natural gas main.

Mr. J--- S. G---, Jr., Property Tax Administrator for [city] Gas & Electric (G&E), sent copies of diagrams of a proposed such facility. We understand that G&E produces the CNG by taking natural gas from G&E's regular distribution system of gas mains which pumps the gas at five pounds per square inch (PSI) of pressure. G&E feeds the natural gas through small lines into a small gas compressor which boosts the pressure to about 3,500 to 4,000 PSI and pumps the gas into a cascade of high pressure storage cylinders. You note that, although Mr. G---'s letter states, "The resulting CNG is stored in a cascade of high pressure storage cylinders or injected directly into vehicles through a fueling post.", you understand that all the gas is pumped into the storage cylinders, and none of it is pumped directly from the compressor to the vehicle tank.

We agree with your conclusion that, when G&E sells equipment to persons who use their equipment to compress the gas, section 6353 applies to exempt G&E's sale of the uncompressed gas. A person who compresses the natural gas would be subject to use fuel tax on the use of the fuel in vehicles operated on highways.

As we discussed earlier, in light of the court's unpublished decision in the case of Sparklett's Drinking Water Corporation v. State Board of Equalization, we believe that the Board also should not attempt to assert tax on the sales by a person who uses the compressor to convert the natural gas to CNG and sells the CNG. As was the case in Sparkletts, the essential mode of delivery is a main, line, or pipe, regardless that some processing of the gas occurs. In the Sparkletts case, the court found that there was no substantial change in the water when the

machine removed impurities. In this case, compressing the gas under pressure does not result in a substantial change in the gas.

We hope this answers your question; however, if you need further information, feel free to contact me directly.

RLD:sr