

**M e m o r a n d u m****330.4020**

To: Van Nuys – Subdistrict Administration (CH)

Date: September 23, 1968

From: Tax Counsel (TPP:LAA) – Headquarters

Subject: Rentals Research &amp; Development

This is in response to your request telephone inquiry concerning the taxability of leases of automatic entry and exit equipment to operators of parking lots and other areas where access is controlled. It is our understanding that the lessor purchases numerous component parts from various suppliers and assembles them into the various pieces of entry and exit equipment. The equipment has been designed and engineered by the lessor, but they manufacture none of the components. Whether the parts are standard parts or manufactured specially for lessor is not known, but is not significant.

There are four variations available: card key operation, coin operation, free entrance operation, and ticket dispenser operation. As an example, the card key operation entrance installation includes a card key receptacle, a “torqscrew” parking gate apparatus, ground treadles and appurtenant metal posts to protect the apparatus. The system is connected electronically so that when a user inserts his coded card key in the receptacle, impulses are sent to the gate apparatus which lift the gate. The car then passes through the gate and over the ground treadles, which sends impulses to the gate apparatus to close the gate. The card key exit apparatus includes a “one-way” steel spring apparatus installed at ground level, two-ground level treadles, an illuminated red octagonal sign indicating to vehicles outside the parking lot “Do Not Enter—Severe Tire Damage.” The steel spring spike apparatus is designed so that cars exiting pass over them without difficulty, but autos attempting to enter through the exit contact a stiff spike, causing tire damage.

To illustrate the assembly required on the various pieces of equipment, the auditor secured a copy of a list of the components of assemblies itemized on the list. The list and schedule each indicate assembly labor involved. The list shows 23 component parts costing \$426.65 with 2 ½ hours of labor at \$3.00 or \$7.50 to assemble for a total of \$434.15. The auditor’s schedule shows that the B-3 hood assembly has 6 components; the rocker arm assembly, 3; the trunion assembly, 14; the motor and brake assembly, 16; the G-300 series control, 18; plus other components. The

labor to assemble these subcomponents, which was included in the \$426.65 above, was \$42.85. thus a more accurate breakdown of the cost would be: Parts, \$383.80; labor, \$50.35 for the total of \$434.15. the equipment is assembled at the lessor's plant and installed at the lessee's premises. The lease signifies that the property shall at all times remain personal property. The apparatus are leased with each party having the option to cancel with 30 days notice.

On these facts, I believe there is no question the rental receipts are subject to sales and use tax. Revenue and Taxation Code Section 6006 (g) includes among those transactions subject to sales tax "Any leases of tangible personal property in any manner or by any means whatsoever, for a consideration,..." unless the lease falls within one of the exceptions listed in the section. Since this is not a lease of motion pictures, linen supplies, household furnishings, or mobile transportation equipment, the only exception under which it might come is section 6006 (g) (5) [ruling 70(c) (2) (E)] as property leased in substantially the same form as acquired as to which tax reimbursement has been paid pursuant to section 6052 or use tax has been paid measured by the purchase price of the property.

In our opinion the property leased in the present case is not in substantially the same form as acquired. The lessor has actually created or produced a piece of equipment from component parts which bore no resemblance to the finished product before assembly. The equipment was engineered and designed by the lessor and thus takes its form, shape and function through the lessor's efforts. There is a significant increase in value as a result of the labor involved in assembly, not only from the stand point of relation of the labor cost to the cost of the parts, but also, I am certain, from the standpoint of increase in value of the finished product over the cost of the components. The amount of labor involved is substantial. This is not a matter of merely clamping or bolting together of previously completed items.

On equipment completed and placed in service after August 1, 1965, on which tax measured by rental receipts is to be asserted, lessor should be credited with any tax paid on components. On equipment completed and placed in service prior to August 1, 1965, the tax would apply on rental receipts on the first renewal after August 1, 1965. since the contracts in question provide for cancellation with 30 days notice, if they were not renewed between August 1, 1965, and August 31, 1965, they would be deemed renewed as of September 1, 1965 pursuant to ruling 70 (c) (3) (A), and all subsequent rental receipts would be taxable. No credit would be allowed for any payment of tax on cost of materials on equipment rented prior to August 1, 1965.

LAA:ph

cc: Los Angeles District – District Administration