

Memorandum

To: Mr. Norman Jung
Staff Tax Auditor, San Jose District

Date: July 15, 1992

From: John L. Waid
Tax Counsel

Subject: **REDACTED TEXT**
Title-Passage Clauses
SR GH REDACTED TEXT

I am writing this in response to your memorandum to the Legal Division of May 7, 1992. You are asking if certain title-passage clauses are presumed to be included in certain government contracts even though they are not included in the documents themselves.

I. FACTUAL BACKGROUND.

You set forth the factual background of your problem as follows:

"The above taxpayer is currently being audited. An issue has arisen in regards to purchases related to U.S. Government contracts. We have questioned several purchases of significant amounts that were purchased for resale by the taxpayer and claimed to be resold to the U.S. Government before use was made by REDACTED TEXT.

"Our examination of the questioned contracts revealed that they do not contain the necessity title clauses. As a result, we are preparing to assess use tax on the taxpayer."

You indicate that the taxpayer contacted its attorneys on this matter. Its question was as follows:

"Revised budget allows equipment to be purchased on a contract that originally did not contemplate equipment purchase -- no title clause in contract. No correspondence from the government regarding title to this equipment. FAR clause may govern below \$5000 but what happens above \$5000?"

You indicate that the attorneys' answer was as follows:

"FAR 45.106(f) requires the inclusion of the property clause at 52.245-5, Alternate I in cost reimbursement research and development contracts with

higher educational institutions. In the absence of specific contract provisions addressing title to equipment costing \$5000 or more, it is presumed that title vests in the federal government." (emphasis in original.)

II. OPINION

Aerospace Corp v. S.B.E. (1990) 218 Cal.App.3d 1300 held that title to overheard items purchased by a federal contractor passed to the federal government prior to use by the contractor when the appropriate title-passage clauses were contained in the contract. (Ibid. at 1315.) As noted by the taxpayer, FAR 45.106(f)(2) requires that the clause at FAR 52.245-5, Alt. I, be inserted in solicitations and contracts when a cost-reimbursement, time-and-materials, or labor-hour contract for the conduct of basic or applied research at nonprofit institutions of higher education or at nonprofit organizations whose primary purpose is the conduct of scientific research when it is contemplated that government property will be furnished to the contractor for the performance of that contract.

We cannot agree with REDACTED TEXT's legal staff. We have previously determined that it does not automatically follow that government property clauses are necessarily included in individual government contracts merely because acquisitions regulations require that such clauses be included with respect to certain kinds of contracts.

As Aerospace makes clear, the governing provisions are to be found in the provisions of the individual contracts as actually executed. It is of course possible that the United States and the contractor could reform the contract, but the new provisions would not be effective against third parties, including the State, for conditions arising prior to reformation.

Here, the facts show that it was not contemplated at the time of contracting that REDACTED TEXT would purchase any equipment. Therefore, the clauses prescribed in FAR 52.245-5 were not required to be, and so were not, included. REDACTED TEXT was later given authority to purchase equipment, but the contract was not reformed. Since the contract did not contain the appropriate title-passage clauses, as called for in Aerospace, there is no accelerated title passage. Only those items that were actually resold to the United States prior to their use by REDACTED TEXT may be considered as having been purchased for resale.

JLW:es

cc: Glenn Bystrom
Mike Hilbert, Aerospace Coordinator, Audit Eval. & Plan.