



STATE BOARD OF EQUALIZATION

(916) 324-4441

March 31, 1989

Mr. A--- H. R---
XXXX C--- B---
---, California XXXXX

Re: SZ -- XX-XXXXXX

Dear Mr. R---:

I have been asked to respond to your letter of February 23, 1989 requesting a legal opinion regarding the possible applicability of sales or use tax to the price difference between the cost of materials purchased by a subcontractor and "the mark-up as selling price of those materials to the general contractor for whom he is employed." Specifically, you describe a situation in which the "subcontractor" of doors and windows transfers these materials to the general contractor at a marked up price and assumes the following duties: works with the architect and builder to estimate material needs, delivers said materials to the building site, "may actually help with the installation", and replaces any damaged or broken doors and windows.

Sales and Use Tax Regulation 1521 (enclosed) provides in pertinent part as follows.

CONSTRUCTION CONTRACT

"Construction contract" does not include:

The furnishing of tangible personal property under what is otherwise a construction contract if the person furnishing the property is not responsible under the construction contract for the final affixation or installation of the property furnished. Regulation 1521(1)(B)2. (Emphasis added.)

CONSTRUCTION CONTRACTOR

“Construction contractor” means any person who, for himself, or in conjunction with or by or through others, agrees to perform and does perform a construction contract. “Construction contractor” includes subcontractors and specialty contractors . . . (Regulation 1521(1)(2).)

MATERIALS

“Materials” means and includes construction materials and components, and other tangible personal property incorporated into, attached to or affixed to real property by contractors in the performance of a construction contract and which, when combined with other tangible personal property, loses its identity to become an integral and inseparable part of the real property. A list of typical items regarded as materials is set forth in Appendix A. Regulation 1521(1)(4) (emphasis added).

APPLICATION OF TAX

In general. Construction contractors are consumers of materials which they furnish and install in the performance of construction contracts. Either sales or use tax applies with respect to the sale of the materials to or the use of the materials by the construction contractor. Regulation 1521(b)(2)(A)1.

The key issue for analysis of the question you raise is whether you are contractually responsible for installation of the materials you provide. It is this contractual responsibility which differentiates the retailer who furnishes materials which will be installed by others from the true subcontractor who both furnishes and installs the materials. The retailer who furnishes material, but does not install it, incurs a sales tax measured by the retail sales price, including markup. The subcontractor, who both furnishes and installs materials, owes tax only on the cost of the materials. In your letter you did not provide information regarding your contractual responsibility. It appears, however, from the information you did provide that you are not contractually responsible for installation, although you may help someone else install the materials.

In Overly Manufacturing Company v. State Board of Equalization (1961) 19 Cal.App.2d 20, the Court of Appeal analyzed a situation that appears analogous to the one you describe in your letter. Overly, the plaintiff, was a licensed construction contractor and manufacturer of door frames and steel doors. Overly entered into contracts pursuant to which it manufactured door frames to specification for various structures and delivered them to the job site where they were incorporated into the structure of the building by the general contractor and others. At times plaintiff had to adjust or rework the frames to facilitate the installation of the doors. Plaintiff later manufactured and installed steel doors in some of the previously installed door frames.

The contracts at issue were all lump sum contracts in which the price of the door frames was not itemized separately from the other charges. The court characterized the contract as one with a "dual nature," in that one part of the contract was for the manufacture and installation of doors and the other part was for the manufacture and sale of door frames. As to the first part there was no controversy. All parties agreed that plaintiff was a construction contractor with respect to the furnishing and installation of the steel doors. As to the second part, the court held that the door frames constituted tangible personal property and the transaction constituted a taxable sale of tangible personal property. In its analysis, on page 23, the court stated ". . . it is clear that the fact that tangible personal property is supplied for the purpose of being included into a structure is not sufficient to classify the supplier as a construction contractor or as a consumer of the materials. He must actually engage in the service of incorporating them into the structure, and the service must be more than merely incidentally performed to accomplish the sale . . . the tax is measure by the price of the frames without deduction for either the cost of labor in manufacturing them or the cost of services in installing them." For tax purposes, title to the door frames passed when the materials were accepted at the job site by the general contractor.

In the case of Hayward Building Material Co. v. State Board of Equalization, (1958) 164 Cal.App.2d 607, the issue before the court was whether Hayward was a construction contractor with respect to its sales of wet mix concrete and asphalt to a general contractor. The court found, however, that the general contractor did no more than order materials for construction from Hayward who was not contractually responsible for its installation. Hayward brought the materials out to the construction site, but its only employee at the site was the truck driver. The court held that Hayward was a retailer and, therefore, obligated for tax on its sales to the general contractor of prepared materials.

As you can see, the answer to your inquiry depends upon whether you are contractually obligated to "furnish and install" materials. If so, you are considered to be the consumer of those materials and only your cost is taxable. The tax on your cost is either paid by you as sales tax reimbursement at the time of purchase or paid and reported directly by you to the Board as use tax.

If you are not contractually obligated to both furnish and install the windows and doors, then you are a retailer of those materials and your entire charge to the general contractor, including any markup, is taxable. Please note, however, that you are entitled to a refund or credit for that part of the charge, if any, attributable to a prior tax-paid purchase. Sales and Use Tax Regulation 1701(a) provides that:

A retailer who resells tangible personal property before making any use thereof (other than retention, demonstration or display while holding it for sale in the regular course of business) may take a deduction of the purchase price of the property if, with respect to its purchase, he has reimbursed his vendor for the sales tax or has paid the use tax. If such a deduction is taken by the retailer, no refund or credit will be allowed to his vendor with respect to the sale of the property.

The deduction under the caption "Tax-paid purchases resold" must be taken on the retailer's return in which his sale of the property is included. If the deduction is not taken in the proper quarter, a claim for refund of tax must be filed.

Please feel free to contact me if you need further clarification of this opinion.

Sincerely,

Stella C. Levy
Tax Counsel

SCL:smt

Enclosure: Regulation 1521