

# Memorandum

**190.1020**

To: Mr. Gary J. Jugum

Date: February 9, 1996

From: Warren L. Astleford

Subject: Sacramento Board Hearings – 2/21/96

Attached are the summaries for my Board hearings on 2/21/96.

Petitioner's claim for redetermination should be denied since petitioner is not a construction contractor within the meaning of Regulation 1521. Instead, petitioner was the manufacturer and retailer of tangible personal property that it provided to a sub-contractor for installation at a particular jobsite.

A construction contractor is a consumer of materials which are furnished and installed in the performance of a construction contract. (Reg. 1521(b)(2)(A).) The meaning of the term "installed" as it relates to construction contracts was explored in Western Concrete Structures, Inc. v. State Bd. of Equalization (1977) 66 Cal.App.3d 543. In Western, the plaintiff contracted with a general contractor to provide shop drawings and the fabrication of post-tensioning tendons. Plaintiff did not unload the tendons nor install or stress the tendons at the jobsite. Plaintiff did, however, inspect and approve the placement of the tendons, provided the equipment necessary to stress the tendons, was contractually responsible for correcting any problems caused by its design, and directly provided all supervision and testing in the installation of its product (since it was the only one with the expertise to do so). Under these facts, the court concluded that plaintiff was a construction contractor within the meaning of Regulation 1521 since it had the ultimate responsibility and control over the final installation of the products it moved to the jobsite.

In this case, petitioner acted only as the supplier of materials under purchased orders issued by the prime contractor. Petitioner would: 1) obtain a quote from a third party contractor who would install the property sold by petitioner; 2) petitioner would communicate that amount

to the general contractor, 3) the prime contractor would then issue a purchase order to petitioner for the bid amount less the installation amount; and 4) the prime contractor would directly contract with the subcontractor at the bid price communicated by the petitioner to the prime contractor. The audit work papers contain various purchase orders from prime contractors only for the purchase of supplies – not installation. There is no documentation specifying that the petitioner was contractually obligated to install the property it sold or that petitioner either supervised the installation of its products or provided the equipment necessary for installation. Petitioner further failed to provide such documentation upon reaudit that it was responsible for installation of the property it sold to the prime contractor. Petitioner fails to meet any of the elements set forth in Western Concrete Structures necessary for a finding that it was responsible for the installation of the property it supplied to its prime contractors during the audit period. For these reasons, the Department requests that petitioner claim be denied.

STATE OF CALIFORNIA

190.1020

BOARD OF EQUALIZATION

In the Matter of the Petition	)	APPEALS SECTION
for Redetermination Under the	)	SUMMARY FOR BOARD HEARING
Sales and Use Tax Law of:	)	
	)	
L. O--- & S--- INC.	)	S- -- XX XXXXXXX-010
dba L. O--- & S---	)	
	)	
<u>Petitioner</u>	)	[city]

Petitioner's representative, --- --- --- ---, Inc., requested in a February 4, 1994 letter (Exhibit A) that the Appeals attorney assigned to this matter be replaced because petitioner's representative believed that the Appeals attorney was strongly disposed to rule in favor of the Board's audit staff. Otherwise, petitioner would waive appearance at an Appeals conference. The Appeals Section, in a March 2, 1994 letter (Exhibit B) declined to reassign this matter. Thus, an Appeals conference was not held, nor was a Decision and Recommendation prepared.

Business: Structural steel fabricator with some construction contracts.

Tax determined for the period 4-1-88 to 3-31-91	\$176,403.58
Reaudit adjustment	<u>- 4,797.95</u>
Proposed redetermination	\$171,605.63
Credit concurred in	<u>300.00</u>
Protested	<u>\$171,905.63</u>
Proposed tax redetermination	\$171,605.63
Estimated interest to February 29, 1996	<u>112,679.33</u>
Total tax and estimated interest	\$284,284.96
Payments	<u>- 60,000.00</u>
Balance	<u>\$224,284.96</u>
Estimated additional monthly interest to accrue March 1, 1996	<u>\$1,116.06</u>

The protested tax is measured by \$2,764,186 representing an understatement of retail sales established on an actual basis.

No penalty was added to the determination.

#### Statement of Unresolved Issue

Whether the evidence establishes that petitioner was contractually responsible for the installation of steel furnished and fabricated by petitioner under lump sum construction contracts.

#### Petitioner's Contention

There are several transactions included in the audit classified as retail sales which are construction contracts.

#### Appeals Section Summary

#### Background

Petitioner entered into contracts which did not state that petitioner was responsible for installation of the steel that petitioner fabricated. Petitioner would issue a bid to a prime contractor including a quoted price from a third party who would be the installing contractor of the steel. The name of the proposed installer and the installer's price quote was communicated to the prime contractor as part of the bid. The prime contractor would then issue a purchase order to petitioner for the bid amount less the installation portion. The prime contractor would issue a purchase order directly to the installing sub-contractor for the amount quoted by petitioner. Petitioner was not responsible for any supervision of the installation. The reason for handling the installation in this manner is that the prime contractor is a union business and petitioner is not. The installing sub-contractors were also union businesses.

Petitioner argues that even though it did not do the physical installation, it was responsible for the installation. Therefore, pursuant to Western Concrete Structures, Inc. v. State Board of Equalization (1977) 66 Cal.App.3d 543, (WCS) it is a construction contractor pursuant to Sales and Use Tax Regulation 1521. Thus, the proper tax liability is the cost of materials installed on lump-sum contracts and not the retail selling price of tangible personal property.

Subsequently, petitioner presented additional documents arguing that certain materials were furnished and installed by petitioner as a construction contractor, not as a retailer. In addition, petitioner argues that 5 transactions were included in the audit twice, extras added to the contract and installed were considered retail sales, and the amount shown as the retail selling price on certain retail sales was overstated.

The Sales and Use Tax Department prepared a reaudit where they deleted the 5 transactions that were duplicated, made adjustments on contracts and extras where petitioner proved that the materials were installed, and allowed an adjustment to one retail sale. No adjustments were made on the remaining transactions due to lack of documentary evidence supporting petitioner's position. The reaudit reduced the understated retail sales by \$77,559 to \$2,764,186.

#### Decision and Recommendation

The Appeals Section recommends that the tax be redetermined in accordance with the reaudit report dated October 10, 1995.

#### Appeals Section's Analysis

A construction contractor is a consumer of materials which are furnished and installed in the performance of a construction contract (Sales and Use Tax Regulation 1521(b)(2)(A)). However, if a fabricator delivers property to a job-site and does not install the property, the fabricator is a retailer (Sales and Use Tax Annotations 190.0240 and 190.0960).

In Western Concrete Structures, Inc., supra, the Court found that there was evidence that WCS was contractually responsible for, and directly provided, all supervision and testing of the installation work performed and that WCS was required to make any necessary corrections in the materials whenever there was a force failure. (Attached as Exhibit C is a copy of page 547 of the Court of Appeal opinion in Western Concrete Structures, Inc., which in footnote 3 details the work performed by WCS.)

The available evidence in this matter does not show that petitioner was responsible for the installation as in Western Concrete Structures, Inc., thus, petitioner is a retailer of tangible personal property and no adjustment is warranted.

Summary prepared by the Appeals Review Section

ARS:me:---  
1-10-95; rev. 11-21-95