



STATE BOARD OF EQUALIZATION

(916) 445-5550

March 5, 1990

Dear _____,

This is in response to your letter dated January 23, 1990. Your former subsidiary, _____ Construction Company, was assessed additional sales tax in a recent audit. This liability arose by virtue of a subcontract _____ had with _____, a prime contractor for the United States Government.

In its contract with _____, _____ certified: "that the tangible personal property purchased from _____ Construction Co. on our Contract No. _____ which will be "Machinery and Equipment" as defined in Regulation 1615 [sic] of the California State Board of Equalization, will be resold by us in the form of tangible personal property to the United States Government."

Regulation 1521, a copy of which was attached to the audit report provided to you, is the regulation that governs this subject (Regulation 1615 was incorporated into Regulation 1521 in 1976). _____ and its subcontractors were United States construction contractors with respect to _____ contract with the United States government. (Reg. 1521(a)(3).) A United States construction contractor is a retailer of machinery and equipment furnished in connection with the performance of a construction contract with the United States government. (Reg. 1521(b)(1)(B).) If you had furnished machinery and equipment pursuant to your contract with _____, then you would have been regarded as selling that machinery and equipment to _____ for resale to the federal government. No tax would apply to your sale since your sale would have been a sale for resale.

However, as stated in the audit report, the auditor concluded that you had purchased materials and fixtures ex tax and used those materials and fixtures in connection with the performance of the contract with the United State government. (For purposes of construction contracts, "materials," "fixtures," and "machinery and equipment" are defined in subdivision (a) of Regulation 1521.) As discussed in subdivision (b)(1)(A) of Regulation 1521, United States construction contractors are regarded as consumers of materials and fixtures which they furnish and install in performance of contracts with the United States government. Since you purchased the materials and fixtures ex tax, use tax measured by purchase price applied to your use on the material and fixtures in performance of the construction contract.

We note that the provision from the contract quoted above states that _____ would purchase for resale such property that is regarded as machinery and equipment for purposes of sales and use tax. We also note that the other provision from the contract that you have provided us states that the contract is based on resale to the government. The parties apparently believe that the items _____ furnished and installed were machinery and equipment. Our audit staff disagrees, concluding that these items were materials and fixtures. If you disagree with this conclusion, you

may file a petition for redetermination within 30 days from the date of mailing to you the Notice of Determination, or you may file a claim for refund after paying the amount assessed.

If you have further questions, feel free to write again.

Sincerely,

David H. Levine
Tax Counsel

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