

M e m o r a n d u m

565.0628

To: Mr. Gary J. Jugum

Date: July 5, 1989

From: David H. Levine

Subject: U.S. Government Contracts – Title Clause Provisions

This is in response to your memorandum dated May 1, 1989. Generally, United States contractors are consumers of materials and fixtures used in the performance of contracts with the United States for construction of improvements on or to real property in the state. (Rev. & Tax. Code § 6384.) In the matter of _____, Hearing Officer Herbert L. Cohen concluded that an accelerated title passage clause in a United States construction contract is effective to transfer title to the United States before use when property is purchased by the contractor out of this state. This would mean that California sales or use tax would not apply to the contractor's acquisition or use of such accelerated title passage provisions, you ask:

“(1) Is ASPR [Armed Services Procurement Regulations] still in existence? Is there now a new FAR (Federal Acquisition Regulations) which may be applicable to both military and non-military U.S. Government acquisitions?”

“(2) Do the acquisition regulations presently in force contain standardized clauses to be utilized in construction contracts providing for passage of title from the contractor to the Government immediately upon acquisition by the contract?”

Title 32 of the Code of Federal Regulations contains regulations promulgated by the Department of Defense. An editorial note at the beginning of the first volume of that title explains that the FAR system went into effect on April 1, 1984, replacing the Federal Procurement Regulations System (FPRS) for civilian contracts (41 CFR subtitle (a), Chapters 1 to 49) and the Defense Acquisition Regulations (DAR) for defense contracts (32 CFR Chapter 1, parts 1 to 39). These provisions apply only to those contracts entered into prior to the adoption of the FAR system. The DAR system had replaced the ASPR system. (See 32 CFR §160.4(b) (ASPR redesignated as DAR with all policies and procedures continuing in force).) Therefore, the ASPR, as well as the DAR, was superseded by the FAR effective April 1, 1984.

Chapter 1 of FAR are government-wide acquisition regulations jointly issued by the General Services Administration, Department of Defense, and the National Aeronautics and Space Administration. Parts 52 to 99 of Chapter 1 include contract clauses and forms. Chapters 2 through 59 are acquisition regulations issued by individual government agencies. Relevant provisions of the first volume of Chapter 1 are parts 12 (Contract Delivery or Performance), 34 (Major System

Acquisition), 35 (Research and Development Contracting), 36 (Construction and Architect Engineer Contracts), 45 (Government Property), and 46 (Quality Assurance), copies of which are attached. The associated contract provisions are at 52.212, 52.236, 52.245, and 52.246, copies of these are also attached.

One provision that provides for title passage is 46.505, Transfer of Title and Risk of Loss. This provision provides that title to supplies passes to the government upon formal acceptance regardless of when or where the government takes physical possession, unless the contract specifically provides for earlier passage of title. Under this provision, title does not pass automatically but rather upon acceptance. This policy is specified in the contract clause at 52.246-16, which is to be used in contracts for supplies, services involving the furnishing of supplies, and R&D contracts when a fixed-price contract is used. The clause does not appear to be applicable to materials or fixtures used in construction contracts.

Provision 45.106(f)(1) requires, with certain exceptions, the insertion of the clause at 52.245-5. Government Property, in contracts when a cost-reimbursement, time-and-materials, or labor-hour contract is contemplated. Subsection (c) of 52.245-5 states:

“(2) Title to all property purchased by the contractor for which the Contractor is entitled to be reimbursed as a direct item of cost under this contract shall pass to the vest in the Government upon the vendor’s delivery of such property.

“(3) Title to all other property, the cost of which is reimbursable to the Contractor, shall pass to and vest in the Government upon –
(i) Issuance of the property for use in contract performance;
(ii) Commencement of processing of the property or use in contract performance; or
(iii) Reimbursement of the cost of the property by the Government, whichever occurs first.”

It appears that his clause would be used in a construction contract. Only title to that property coming within subsection (c)(2) would pass to the Government upon the vendor’s delivery. Even if this provision had been the actual provision involved in the _____ case, I note that the hearing officer did not actually review the contract at issue. The auditor did not contest petitioner’s assertions on this issue and the hearing officer accepted the auditor’s concession. It is entirely possible that the auditor misconstrued the title passage provisions of the contract. For example, title to some of the property at issue may have passed to the Government in California under subsection (c)(3) and would have been properly subject to tax under Revenue and Taxation Code Section 6384.

DHL:jb

cc: Mr. E. L. Sorenson, Jr.