



**STATE BOARD OF EQUALIZATION**

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August 23, 1993

Mr. R--- B. S---  
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--- ---, CA XXXXX

Dear Mr. S---:

This is in reply to your April 27, 1993 letter regarding the application of sales tax to charges to and by your client for tools and computer programs under the following facts you provided:

“The client enters into contracts to manufacturer (sic) and sell printed circuit boards and other electronic items (together referred to herein as “boards”) to the customers. These boards are typically resold by the customers since they are component parts of the products the customers sell. On occasion, the customers are the end users of the boards. The client reports and collects tax on the sales of the boards to its customers unless a sale is supported by a resale certificate or the sale is exempt for some other reason (interstate, commerce, etc.).

“Our client uses tools in order to manufacture and test the boards. These tools are comprised of two general classes of items: (1) stencils and other items which are used during the manufacturing process, and (2) test equipment which is used to determine if the boards meet predetermined specifications. Computer programs are needed for use with both of these types of tools. Some of the equipment programs are loaded into the clients’ computers in the manufacturing area and used to direct the clients’ equipment to perform certain functions during the manufacturing processes. Other computer programs are loaded into the clients’ computers and used in conjunction with the test equipment. These latter programs determine if all of the circuits are operative and function as intended. The tools and computer programs are used at the clients’ California location in the manufacturing process or in the testing of the boards.

“The clients’ customers order these tools and computer programs when a new board is first ordered. The charges for the tools and computer programs are listed separately from the charge for the boards on the customers’ purchase orders. Most of the tools and computer programs are manufactured or prepared by outside vendors or authors who sell them to our client. Some of the tools and computer programs are manufactured and written by the clients’ employees. The clients’ customer’s purchase orders include provisions that all tooling and programs ordered by the customer belong to the customer. In almost all cases, the tooling and computer programs physically remains at the manufacturing facilities of our client, even though title to the tooling and programs has passed to the customer. The charges for the tools and the programs are listed separately from the charge for the boards on the clients’ sales invoices.

“The charge for the tools is considered taxable and our client has in the past collected and reported sales tax on those amounts. The charge to customers for computer programs are considered exempt because the programs are custom computer software under Rev. & Tax Code § 6010.9 because they are prepared to the special order of the customer.

“In order to confirm our client’s understanding with its customers, our client intends to incorporate the following title clause in the quotations it gives to its customers:

The title to all tools and computer programs purchased or manufactured specifically for this contract which are used in the production or the testing of products passes to the customer prior to the time the tools and computer programs are used by [seller].”

Given this information, you asked for our opinion that sales of tooling and computer programs to your client for specific contracts with its customers will not be subject to sales tax such that your client may issue a resale certificate or, alternatively, if your client has purchased the property tax paid, your client may take a tax paid purchases resold deduction.

We agree that, under the facts you described, we consider your client transfers title to the tools and computer programs to its customers prior to use in the manufacturing process. Your client may issue a resale certificate to its vendor to purchase the tools ex-tax. When your client has paid sales tax reimbursement to the vendor and transfers the tools to the client prior to use your client may take a tax paid purchases resold deduction.

As to the custom computer programs, we assume that the programs are not in existence at the time your client contracts to supply the programs to its customer; that is, your client contracts with the customer to provide a custom computer program to the customer’s special order and then subcontracts with another person who creates the program to the special order of your client’s customer.

In such a case, we also agree with your conclusion that the sales tax does not apply to your client's charge to the customer for the custom computer programs.

We hope this answers your question; however, if you need further information, feel free to write again.

Very truly yours,

Ronald L. Dick  
Senior Staff Counsel

RLD:plh