M e m o r a n d u m

190.2435

To: Headquarters – Principal Tax Auditor Date: March 29, 1967

From: Tax Counsel (EHS:EDM) - Headquarters

Subject: G--- Corporation
---, CA XXXXX S- -- XX XXXXXX

K---, Incorporated nonpermittee
------, New York

This is in reply to your memorandum of January 17, 1967, in which you ask for our opinion in respect to the application of the tax in connection with the sale of materials and equipment, etc., used in connection with the construction of a "K--- C--- C--- System" in [city], California, for the G--- Corporation (herein, "B" corporation) by K---, Inc., (herein, "A" corporation).

After reviewing the attached materials relating to this account, it appears that "A" corporation, a New York corporation which does not hold a California seller's permit, entered into a contract with "B" corporation, a California permittee, under which "A" corporation agreed "to supply and install" the above mentioned "cooking system" (i.e., digester shell unit, etc.) for "B" corporation at the lump-sum price of $1,500,000. The contract provides, among other things, that "A" corporation will furnish the cost of labor and materials in fabricating the "Continuous Cooking System" and in installing it, except that "B" corporation was to provide the foundations including the reinforcing steel and anchor bolts necessary for installing the "digester unit."

The major element of this installation is the digester, which is a unit 11 feet in outside diameter and 160 feet high. We understand that in erecting the "digester shell unit," it is attached to a foundation by means of large anchor bolts. Inasmuch as the equipment specifications for "A" corporation's "digester shell unit" includes shop fabrication, we assume that the particular unit was designed, fabricated, and tested at the fabricator's out-of-state factory prior to its shipment to "B" corporations' California jobsite for final field erection. All items of property are shipped f.o.b. [city], California. In addition to the supply and erection of the digester unit and the supply of the basic mechanical components, the selling price contains certain engineering services as listed on page 9 of "A" corporation's initial proposal of February 5, 1964. The cost of the materials and equipment used in manufacturing the digester unit have not yet been ascertained. We assume that, due to its size, it was probably dismantled to

facilitate shipment to the California jobsite. There it was installed by "A" corporation, under the supervision of "A" corporation's contractors, on a foundation supplied by "B" corporation. Installation was to commence between March 1, 1964, and April 15, 1964, and be completed in four months.

On these facts, it is out tentative opinion that, as to "A" corporation, the "digester shell unit" is tangible personal property and the transaction constituted a sale of tangible personal property in California by "A" corporation to "B" corporation within the meaning of sales and use taxes ruling 11(c). Since the contractor was the manufacturer of the fixture (i.e., digester unit) it furnished and installed under its lump-sum construction contract, the tax applies to the retail selling price which, in this case, would be the prevailing price at which similar fixtures ready for installation would be sold to contractors.

It should be noted, however, that "A" corporation is not a retailer of those items of tangible personal property it installs but does not furnish under the construction contract.

It has been our view that, when a seller in under a duty to install specific property after delivering it to the buyer's jobsite under a contract which terms are "f.o.b. point of destination," the title to the property will not be regarded as passing prior to delivery. Since "A" corporation is required, under the contract, to install certain equipment and materials upon delivery to the jobsite, and the agreement provides that the property is to be shipped f.o.b. [city], California (point of destination), it would appear that title to the property does not pass prior to delivery to the buyer's jobsite. It should be mentioned in this connection that any charge for transportation of the goods is one which occurs prior to the sale and, thus, is subject to sales tax under § 6012(c) of the California Sales and Use Tax Law.

Also, since the contract provides that the "digester shell unit" erection will commence between March 1, 1964, and April 15, 1964, it is clear that it will be delivered to the buyer's jobsite, at the latest, by April 15, 1964. On these facts, title to the digester unit would pass prior to the attempt on May 11, 1964, to modify the original contract terms. Even though parties may change their rights as between themselves, a self-serving change in terms of an existing contract does not affect the rights of a third party (i.e., State of California) which vest on the making of the agreement of sale. Accordingly, it is our opinion that the state's right to the tax on the "sale" of the digester unit could not be divested by a subsequent modification of the contract terms. The May 11, 1964, modification by the parties provided that title pass at the point of shipment. We assume the modification became effective between the parties sometime in May of 1964. Since the modification occurred prior to the time <u>all</u> <u>other</u> equipment under the contract was to be delivered (six to eight months from the date of order – January 31, 1964), it appears that title to <u>this</u> equipment had not yet passed at the time the parties sought to modify their agreement. Therefore, it is our belief that as to <u>this</u> equipment, the modifications affected not only the rights and duties between the parties but also any "rights" of a third party (State of California).

Inasmuch as title to this equipment passes to the buyer prior to the transportation of the property to the jobsite, any separately stated charges for such transportation would be excluded from the tax.

In giving our opinion, we have assumed that "A" corporation purchased this equipment from California vendors ex tax and furnished their vendors with "B" corporation's seller's permit number. The letter from "B" corporation to "A" corporation, dated August 7, 1964, would seemingly infer "B's authorization to use its seller's permit number in purchasing property from California vendors ex tax for resale.

Inasmuch as "A" corporation does not appear to be "B" corporation's duly authorized agent in purchasing this property, we believe that there was an improper use of "B" corporation's seller's permit. It is our opinion, however, that "A" corporation's use of "B" corporation's seller's permit number does not require the conclusion that "B" corporation, rather than "A" corporation, is the proper taxpayer.

Prior to the parties' modification of the original contract, it appears that "A" corporation would be the consumer of any materials it uses in fulfilling its construction contract and, as such, must pay tax measured by the cost of the materials to it. However, after the modification, "A" would be the retailer for any tangible personal property (i.e., equipment, etc.) sold to "B" corporation in California. In addition, since we have tentatively concluded that "A" corporation is the retailer of the "fixture" it furnishes and installs for "B" corporation under a lump-sum construction contract, it would appear that "A" corporation must pay sales tax on the "sale" of the fixture to "B" corporation.

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