STATE OF CALIFORNIA

315.0328

STATE BOARD OF EQUALIZATION
LEGAL DIVISION (MIC:85)
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January 28, 1994

K--- D. M---, Tax Manager
T--- P--- Co.
c/o Tax Department
XXXX --- --- ---
--- ---, CA XXXXX

Re: Application of Tax
Regulations 1546/1655
Various Issues
Third Party Service Repair Contracts

SY -- XX-XXXXXX

Dear Ms. M---:

This is in response to your facsimile dated November 19, 1993, containing a number of questions regarding the application of sales and use tax to third party service/repairs that you perform for your customers. In your letter, you state:

> "Our company performs third party service/repair calls for customers. These customers hire us because they do not have any employees located in the state where the work is done.
>
> "An example would be one of our customers located in TN. They have customers throughout the US, however, they do not have any employees or property in any state other than TN. Therefore, when their customers need any work done outside the state of TN, they hire our company to handle the job."

You have listed various issues which we discuss below.

Third/Party Service Repair Contracts - General Discussion

You indicate that your customers who are located outside of this state and do not have any employees in California hire T--- to perform third party repairs for their products that are located in California. You do not indicate what items are being repaired or explain the terms of your contracts with your customers. We assume that you are hired to perform repairs on products that are covered by some type of maintenance agreement. We further assume that you charge your customers based on each repair job, and that you do not perform repairs pursuant to maintenance agreements between you and your customers.

The rules applicable to your repairs are set forth in Regulation 1546(b)(1) and (b)(2):

> "(1) If the retail value of the parts and materials furnished in connection with repair work is more than 10 percent of the total charge, or if the repairman makes a separate charge for such property, the repairman is the retailer and tax applies to the fair retail selling price of the property.
>
> "If the retail value of the property is more than 10 percent of the total charge, the repairman must segregate on the invoices to his customers and in his records the fair retail selling price of the parts and materials from the charges for labor of repair, installation, or other services performed. "Total charge" means the aggregate of the retail value of the parts and materials furnished or consumed in making the repairs, charges for installation, and charges for labor of repair or other services performed in making the repairs, including charges for in-plant or on-location handling, disassembly and reassembly. It does not include pick-up or delivery charges.
>
> "If the retailer does not make a segregation, the retail selling price of the parts and materials will be determined by the board based on information available to it.
>
> "(2) If the retail value of the parts and materials furnished in connection with the repair work is 10 percent or less of the total charge, as defined in (b)(1) above, and if no separate charge is made for such property, the repairman is the consumer of the property, and tax applies to the sale of the property to him."

Thus, assuming you separately state your charges for the parts or the retail value of the parts you furnish in connection with the repairs is over 10 percent of your total charge, you are regarded as selling the parts to your customer. If that sale is at retail, you owe sales tax measured by your charges for the parts (or the retail value of the parts if you make no separate charge). Your charges for repair labor are not subject to sales tax. If your sale of the parts is for resale, no tax applies to your charges.

A person obligated under an optional maintenance agreement to furnish parts, materials, and labor necessary to maintain the property is the consumer of such parts and materials. (Regs. 1546(b)(3)(C), 1655(c)(3).) Thus, if your customers contract for your repairs because they are obligated pursuant to optional maintenance agreements, they are consumers of the parts you sell, meaning that your sales of parts to them are at retail. Sales tax applies to your charges for those parts.

A person obligated to furnish parts, materials, and labor necessary to maintain the property under a mandatory maintenance agreement is regarded as the retailer of the parts furnished and may purchase such parts for resale. (Regs. 1546(b)(3)(B), 1655(c)(2).) Thus, if your customers contract for your repairs because they are obligated pursuant to mandatory maintenance agreements, they are the retailers of the parts they purchase from you, meaning that your sales of the parts to them are nontaxable sales for resale.

Subdivision (b)(3)(A) of Regulation 1546 and subdivision (c)(1) of Regulation 1655 explain the difference between mandatory maintenance agreements (including mandatory warranties) and optional maintenance agreements (including optional warranties). Copies of these regulations are enclosed.

Transportation Charges

Transportation charges are excluded from the measure of tax under certain conditions. You do not indicate whether the freight charges you mention are for delivery by common carrier or your own facilities. Regulation 1628(a) explains the application of tax when the transportation is by common carrier. Regulation 1628(b)(2) describes when certain charges for delivery by a retailer's own facilities are nontaxable. Sales and Use Tax Regulation 1628 provides in part:

> "(a) TRANSPORTATION BY CARRIER. Except as provided in paragraph (c) below, in the case of a sale, whether by lease or otherwise, tax does not apply to 'separately stated' charges for transportation of property from the retailer's place of business or other point from which shipment is made 'directly to the purchaser,' provided the transportation is by other than facilities of the retailer, i.e., by United States mail, independent contract or common carrier. The place

where the sale occurs, i.e., title passes to the customer or the lease begins, is immaterial, except when the property is sold for a delivered price or the transportation is by facilities of the retailer, as explained in (b) below. The amount of transportation charges excluded from the measure of tax shall not exceed the cost of the transportation to the retailer.

"Transportation charges will be regarded as 'separately stated' only if they are separately set forth in the contract for sale or in a document reflecting that contract, issued contemporaneously with the sale, such as the retailer's invoice. The fact that the transportation charges can be computed from the information contained on the face of the invoice or other document will not suffice as a separate statement. If a separately stated charge is made designated 'postage and handling' only that portion of the charge which represents actual postage may be excluded from the measure of tax.

"Property will not be considered delivered 'directly to the purchaser' if it is shipped to the retailer, to the retailer's agent or representative, or to anyone else acting in the retailer's behalf. Any separately stated charges by the retailer for the transportation of property to, rather than from, the retailer's place of business, or to another point from which the property will then be 'delivered directly to the purchaser,' are included in the measure of tax. Such charges represent incoming freight and are taxable as part of the cost of the property sold by the retailer.

"....

"(b)(2) IN GENERAL. Except as provided in paragraph (c) below, when transportation is by facilities of the retailer or the property is sold for a delivered price, tax applies to charges for transportation to the purchaser, unless (a) the transportation charges are separately stated, (b) are for transportation from the retailer's place of business or other point from which shipment is made directly to the purchaser, and (c) the transportation occurs after the sale of the property is made to the purchaser. When the sale occurs before the transportation to the purchaser commences, the tax does not apply to separately stated charges for the transportation. The amount that may be excluded from the measure of the tax cannot exceed a reasonable charge for transportation by facilities of the retailer or the cost of transportation by other than facilities of the retailer."

Two conditions for transportation charges to qualify as nontaxable which are applicable in all cases are that the charge be for final transportation of the property directly to the purchaser and that the charge be separately stated to the purchaser. Transportation charges are not "separately stated" unless they are specifically set forth in the contract of sale or in a document reflecting the contract such as an invoice. Without more information about your freight charges, we are unable to determine whether they may be excluded from the measure of tax.

Sales to the Government

You ask whether T--- should be collecting and submitting tax when the customer is the federal government, state government or a commercial business. There is ***no*** exemption from sales or use tax for sales of property to persons who consume that property in the performance of contracts with the United States (such persons are commonly referred to as United States contractors). When a seller sells tangible personal property to a person who will consume that property in the performance of a contract with the United States, that sale is subject to sales or use tax. Additionally, there is no exemption from sales or use tax for persons who sell tangible personal property in California to state governments.

Although a person's sales of tangible personal property directly to the United States are exempt from sales tax (Rev. & Tax. Code § 6381.), this exemption does not apply here since you will not be making any sales to the United States. Rather, your sales of property furnished in making your repairs will be subject to sales tax, measured by your charges for such property (or the retail value thereof), unless your sale is a sale for resale.

As discussed above, you are regarded as making sales for resale of property that you sell to persons who are obligated to furnish such property under a mandatory maintenance agreement. Your sales of property (as part of your repairs) to such persons would not be subject to tax without regard to the identity of those persons' customers. On the other hand, as also discussed above, you are regarded as making taxable retail sales when you sell property (as part of your repairs) to persons who are obligated to furnish such property under an optional maintenance agreement. Again, this is true without regard to the identity of the person covered by the optional maintenance agreement, whether the federal government, a state government, or a commercial business.

Resale Certificates Issued by Businesses not holding a California Sellers permit.

You also inquire about accepting resale certificates from your customers even though they do not have California seller's permits and would state that on their certificates. If a purchaser is not required to hold a seller's permit because the purchaser makes no sales in this state, the purchaser may issue a resale certificate which includes an appropriate notation to that effect in lieu of a seller's permit number (Reg. 1668(b)(1)(C)). Since your customers do not make any sales in California, you may accept their timely and valid resale certificates which

contain that explanation in lieu of a seller's permit number if you do so in good faith. Under the specific circumstances of this case, the resale certificate should state the specific basis for regarding the parts as purchased for resale (e.g., furnished pursuant to a mandatory warranty). Of course, if you have reason to know that such explanation is not correct, you would not be regarded as accepting the certificate in good faith.

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

Sincerely,

Gerald Morrow
Tax Counsel

Enclosures: Regulations 1546, 1614, 1628, 1655 and 1668

cc: --- --- - District - Administrator
--- --- - District Administrator