

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

330.4165
12/8/80

In the Matter of the Petition)
for Redetermination Under the) DECISION AND RECOMMENDATION
Sales and Use Tax Law)
) No. SR ----
)
)
)
Petitioner)

The above-entitled matter came on regularly for hearing on Thursday, November 6, 1980 in Inglewood, California before Susan M. Wengel, Hearing Officer.

Appearing for Petitioner: ----

Appearing for the Board: Robbin E. Blomquist
Tax Auditor III

Protested Item

The petitioner has filed a petition for redetermination of a tax deficiency determination issued on February 26, 1980, for the period July 1, 1974 through September 30, 1978. The protest involves tax determined on the following audit item:

Audit Item B: Taxable Measure Understated. Leases subject to tax on lease receipts rather than cost (cost of materials reported) as they were leased in the same form as acquired.

$$\$235,864 - \$53,347 = \underline{\$182,517}$$

Contentions of Petitioner

The items leased were leased in substantially the same form as acquired and consequently the tax was properly reported on the petitioner's cost.

Summary of Petition

The petitioner is a corporation which engaged in the manufacture, sale, and rental of temporary electric power distribution units and cables. It also rented portable diesel generators.

During a routine audit the Board's audit staff concluded that the leases of the following items were continuing sales, and as such should have been reported based on rental receipts:

1. Temporary electric power distribution boxes.
2. Strings of lights.
3. Portable electric power distribution boxes.
4. Power distribution centers.
5. Quartz flood lights.
6. Temporary power distribution panels.
7. High rise cable.

All the generators were considered to have been leased in substantially the same form as acquired and were held to have been reported properly.

The petitioner contends that the power cables, which represent approximately half of the rentals, are clearly leased in substantially the same form as acquired. The petitioner contends that the bulk of the value lies in the cable itself and that merely cutting it to certain lengths and attaching connections at each end does not materially affect the item leased. Apparently the petitioner purchases large spools of insulated copper cable which are cut into various lengths from 25 feet to 200 feet. Also, some small connections are cut to make various adaptors. Then connectors are placed on each end of the cable which enables the cables to be attached to the power distribution boxes (also made by the petitioner) and to the various electrical equipment. Some cables have one end left open so that the cable may be attached directly to power utilities.

The audit staff concluded that the cable as well as the other items listed were not leased in substantially the same form as acquired. The cutting and attachment of connectors materially affected the cables as what the lessees sought was a completed cable with the necessary connections.

The petitioner further contends that in the prior audit the Board accepted their reporting methods as correct. It appears that in the prior audit the auditor was not aware that the petitioner was manufacturing the items rented. The auditor apparently believed that the petitioner was a tax-paid lessor who had through oversight failed to pay tax on rental inventory for part of the audit period. Nowhere in the auditor's comments was any reference made to "manufacture".

The petitioner contends that they relied on this prior audit and object to the imposition of the interest.

Analysis and Conclusion

The petitioner has stated that because over half of their manufactured equipment was sold, all the materials were purchased ex-tax. Once it was determined that a particular item was to be leased, tax was paid on the cost of the materials used to manufacture that item. The petitioner relied on Sales and Use Tax Regulation 1660(c) (2) which provides that:

"No sales or use tax is due with respect to the rentals charged for tangible personal property leased in substantially the same form as acquired by the lessor, or by his transferor, as to which the lessor or transferor has paid use tax measured by the purchase price ... "

Revenue and Taxation Code §6006(g) defines a sale to include any lease of tangible personal property for a consideration. All leases which meet the definition of "sale" and which provide the

lessee with possession of the property in California are considered to be continuing sales in this state by the lessor. (Regulation 1660 (b) (2).) The measure of tax is the rents payable. (Regulation 1660(c) (1).) As the tax is a use tax upon the use in this state of the property by the lessee, the lessor must collect the tax from the lessee at the time the rentals are paid.

If, however, as the petitioner contends, the property is leased in substantially the same form as acquired, the lease would be excluded from the definition of sale and would not be treated as a continuing sale. (Revenue and Taxation Code §6006(g) (5).)

The facts show that the petitioner does manufacture the seven items listed above .. These items, including the cable, are not leased in substantially the same form as acquired. Even the cable has to be cut and have a connector placed on at least one end of the cable before the cable is .of any value to the lessee.

Likewise, the fact that the reporting error was not discovered in the prior audit cannot change this recommendation. The Board cannot in the absence of specific statutory authority exempt a tax liability. *Pacific PipeZine Company v. State Board of Equalization*, 49 c. 2d 729 (1958).

Revenue and Taxation Code §6482 provides that the amount of the determination shall bear interest at the rate of one percent per month. The Board has no authority to excuse the interest. No credit interest for the tax paid on the materials has been shown as tax was only asserted on the net difference between the amount owed based on rentals payable and the amount paid based on the petitioner's cost.

Recommendation

It is recommended that the tax be redetermined without adjustment.

Susan M. Wengel, Hearing Officer

Date

Reviewed for Audit:

Principal Tax Auditor

Date