STATE BOARD OF EQUALIZATION
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June 20, 1994

Mr. R--- J. F---, President
F--- & A---
XXXX --- --- Highway, Suite XXX
---, CA XXXXX-XXXX

Dear Mr. F---:

This is in response to your letter dated April 4, 1994. You ask that we answer a number of questions with regard to the application of sales and use tax.

Your first scenario is as follows:

> "A CA manufacturer purchases a piece of capital equipment from a CA seller. The purchaser visits the seller's facility to sign-off on the equipment prior to delivery. The sign-off is the purchaser's approval that the equipment being shipped meets the purchase specification, however, full title will not vest in the purchaser until final acceptance. The equipment will be delivered and installed at the purchaser's plant where final testing with 'live' chemicals and manufacturing materials will confirm proper equipment operation. Successful on site testing will be the basis for final acceptance and title passage. In this situation, is separately stated installation and final testing with live chemicals exempt from tax?"

All charges from the retail sale of tangible personal property are subject to sales or use tax unless there is a specific statutory exclusion. (Rev. & Tax. Code §§ 6011, 6012.) The exclusion relevant here is for the price received for labor or services in installing or applying the property sold. (Rev. & Tax. Code §§ 6011(c)(3), 6012(c)(3).) The exclusion for installation is applicable only to charges for attachment of the purchased property (BTLG Annot. 435.1640 (11/30/66)), and does not apply to charges for testing. (BTLG Annot. 295.1800 (1/23/50).) Thus, charges for testing are taxable, while charges for actual installation are not.

Your second scenario is as follows:

> "A CA purchaser contracts with a CA computer equipment company for the delivery, installation and configuration of various utility (fax, modem, video, graphics, etc.) boards. The boards are placed in the purchaser's computers by the

> seller's service technician. The technician will open the computer chassis, position the new board, complete the required hook-up, establish the configuration of the computer to accept the board, test the board's function in the computer and close the computer chassis."

For purposes of this analysis we assume that the computer is a new computer and not a used computer which is being upgraded or repaired.

You ask whether separately stated charges for this process qualify as nontaxable installation. You also ask whether the answer changes if the installer is someone other than the seller's employee. You further ask whether the conclusion changes if the installer (someone other than the seller) is contracted for directly by the purchaser.

Installation must be distinguished from fabrication, which would include any step in the manufacturing process of tangible personal property. Tax applies to charges for producing, fabricating or processing of tangible personal property, whether the property is provided by the seller, or instead is provided by the consumer, either directly or indirectly. (See, e.g., Reg. 1526(a).)

Your letter indicates the technician will open the computer chassis, place the utility boards in the purchaser's computer, position the new board, complete the required hook-up, and establish the configuration of the computer to accept the board.

This procedure is a step in providing the final product of a computer with the desired boards. If the described procedure is being performed by the seller before title passes to the purchaser the entire procedure is regarded as a step in the manufacturing process. All gross receipts from that sale are subject to tax, including charges for the described procedure. Even if title to the computer passes to the purchaser prior to the described procedure, the procedure would be a sale under Revenue and Taxation Code section 6006(b) and the charge would be taxable on that basis. The same result is reached whether the person performing the procedure were employed by the seller or whether the purchaser directly contracted with someone other than the seller.

Your third scenario is as follows:

> "A CA purchaser contracts with a CA computer supply company for the delivery, installation and configuration of laser printers. The printers are connected to the purchaser's computers by the seller's service technician. In conjunction with the hook-up, the technician also services (adds toner), tests, and calibrates the new printer.
>
> "1. If separately stated, would this service qualify as exempt installation? If not, explain.

"2. Does the answer change if the installer is not the seller's employee?

"3. Does the answer change if the non-seller installer is contracted for by the purchaser directly?"

As stated above, the installation exclusion is only applicable to charges for attachment of the purchased property and is not applicable to charges for testing. Thus, charges for testing and calibration are taxable, while charges for actual installation are not. Assuming the configuration did not constitute fabrication, it would be installation as would the adding of toner. That the seller contracts with a third party for this work does not change the result. However, if the purchaser contracts directly with a third party unrelated to the sale of any tangible personal property, and no fabrication is involved, none of the charges would be taxable.

We do not address your fourth scenario which relates to research and developments contracts. As you correctly point out, these issues are currently under review.

Your fifth scenario is as follows:

"The Board has generally taken the position that optional equipment maintenance contracts are not taxable. I understand this to mean that an agreement for repair or maintenance labor and parts invoiced as an all inclusive amount are not subject to sales tax. The seller is subject to use tax on the parts consumed in the completion of any equipment servicing. If the seller sends the purchaser an invoice for the contract with the following lines:

"Maintenance contract	1 year	1,000.00
Tax on parts (est.$300)		24.75
Amount due		1,024.75

"What is the appropriate argument for the purchaser to use in challenging this invoice? Assume that the maintenance contract is silent on this issue of tax"

If a retailer collects tax reimbursement on an amount that is not taxable, it would be collecting "excess tax reimbursement". (Reg. 1700(b)(1).) Regulation 1700(b)(2) explains that any excess tax reimbursement must be refunded by the retailer to its customer. If the excess tax is not refunded to the customer it must be paid to the Board.

A person obligated to furnish parts under an optional warranty is the consumer of the materials and parts furnished and tax applies to the sale of such items to that person, or that person's use. (Reg. 1655(c)(3).) Thus, as a consumer, the person furnishing and installing parts pursuant to an optional warranty is not selling tangible personal property to the customer. Since it is not making a sale of tangible personal property, it does not owe sales tax on that transaction. Since it does not owe sales tax, it cannot collect "sales tax," "sales tax reimbursement," "use tax," or "tax" from the customer. If it does so, it is collecting excess tax reimbursement. Under

such circumstances, the warrantor must refund such amounts to the customer. If it does not, it must pay such amounts to the Board. We would not allow a warrantor to continue to collect such excess tax reimbursement.

If we can answer any other questions please feel free to write again.

Very truly yours,

Rachel M. Aragon
Staff Counsel

RMA:sr

cc: San Francisco District Administrator