

**STATE BOARD OF EQUALIZATION**

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August 4, 1992

Mr. REDACTED TEXT

Re: REDACTED TEXT
Federal Construction Contractors

BURTON W. OLIVER
Executive Director

Dear Mr. REDACTED TEXT:

I am writing this in response to your Letter of June 4, 1992, to the Legal Division. You asked for advice regarding the Board's rules on the application of sales tax to the type of contract involved herein.

I. FACTUAL BACKGROUND

You state the factual background of your problem as follows:

"Our customer, COMPANY A, has purchased from our firm sacked REDACTED TEXT dried sand for shipment, prepaid via motor carrier to COMPANY A, REDACTED TEXT, California.

"Our customer invoice included a charge for 8¼% state and local sales tax. This customer is refusing to pay the sales tax charge citing that the federal government takes title to the property directly from vendors."

You attached to your letter a copy of one dated April 2, 1992, which you received from REDACTED TEXT, COMPANY A. She explained her claim that COMPANY B's sales to COMPANY A are exempt from tax as follows:

"COMPANY A is a captive contractor to the U.S. Department of Energy (DOE) under contract REDACTED TEXT. We cannot perform any other work without DOE approval.

"The contract contains numerous clauses of the Department of Energy Acquisition Regulations (DEARs). They include DEAR 970.5204-21, which states that the Federal Government takes title to property directly from our vendors (you) and DEAR 970.5204-16 which states that the government holds title to the money in our bank account until it is paid to the payees of our *checks."

"The net effect, which we have tried to explain on our purchase order form, is that you did not sell anything to us; your goods passed directly to the Federal government and were paid for with their funds."

The Application for Seller's Permit and Registration as a Retailer of COMPANY B states that it is a manufacturer of cement, ready-mix concrete and aggregates. We assume from the fact that the product in question is dried sand, that COMPANY A is buying it for use in the performance of a contract or contracts with the United States for the construction of improvements on or to real property in this state.

II. OPINION

A. Sales and Use Tax Generally.

In California, except where specifically exempted by statute, Revenue and Taxation Code Section 6051 imposes an excise tax, computed as a percentage of gross receipts, upon all retailers for the privilege of selling tangible personal property at retail in this state. (Unless otherwise stated, all statutory references are to the Revenue and Taxation Code.) "[I]t shall be presumed that all gross receipts are subject to tax until the contrary is established. The burden of proving that a sale of tangible personal property is not a sale at retail is upon the person who makes the sale ..." (§ 6091.) "Exemptions from taxation must be found in the statute." (Market St. Ry. Co. v. Cal. St. Bd. of Equal. (1953) 137 Cal.App.2d 87, 96 [290 P.2d 201.]) The taxpayer has the burden of showing that he clearly comes within the exemption." Standard Oil Co. v. St. Bd. of Equalization (1974) 39 Cal.App.3d 765, 769 [114 Cal.Rptr. 571].)

B. Taxation of Federal Construction Contractors

Regulation 1521(b)(1)(A), interpreting and implementing Sections 6007.5 and 6384, provides for the application of sales and use tax to sales to United States construction contractors as follows:

"United States construction contractors are consumers of materials and fixtures which they furnish and install in the performance of contracts with the United States Government. Either the sales tax or the use tax applies with respect to sales of tangible personal property (including materials, fixtures, supplies, and equipment) to contractors for use in the performance of such contracts with the United States for the construction of improvements on or to real property in this state. The fact that the contract may provide principally for the manufacture or acquisition of tangible personal property is immaterial. The sales tax, but not the use tax, applies even though the contractor purchases the property as the agent of the United States."

(Sales and Use Tax Regulations are Board promulgations which have the force and effect of law.)

C. Tax Consequences to COMPANY B

Presumably the dried sand is located in California when the sale takes place. (See, §6010.5.) As it is delivered to the purchaser in California, the applicable tax is the sales tax.

Pursuant to the above authority, COMPANY A is the consumer of the dried sand that it purchases to carry out its contract with the United States. We cannot agree with COMPANY A's claim that the United States is being taxed in this circumstance. COMPANY A is not selling the dried sand to the United States in the form of tangible personal property, but, under the facts as we have assumed them, is using the sand itself in the performance of a contract for the improvement of real property in California. As pointed out by the courts, in federal construction projects the incidence of the tax falls on the contractor and not the United States. (Washington v. United States (1983) 460 U.S. 536, 539 [103 S.Ct. 1344, 75 L.Ed.2d 264].) In re Howell (9th Cir. 1984) 731 F.2d 624, 627.) Federal construction contractors are not "so assimilated by the Government as to become one of its constituent parts." (United States v. New Mexico (1982) 455 U.S. 720, 737 [102 S.Ct. 1373, 71 L.Ed.2d 580].) The fact that COMPANY A uses federal funds to pay its vendors does not convert the tax on COMPANY A's vendors into a tax on the United States itself. (Ibid. at 734.) Therefore, COMPANY B was correct in applying tax to this sale to COMPANY A.

For your information, I have included a copy of Regulation 1521. I hope the above discussion has answered your question. If you need anything further, please do not hesitate to write again.

Sincerely,

John L. Waid
Tax Counsel

JLW:es

Enclosure: Regulation 1521

bc: Mike Hilbert, Aerospace Coordinator, Audit Eval. & Plan.