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August 20, 1993

Mr. REDACTED TEXT

Re: FR GH REDACTED TEXT
Sales to Defense Contractors

Dear Mr. REDACTED TEXT:

I am responding to the letter you wrote to the Legal Division on May 25, 1993. I apologize for the delay. You ask for an opinion regarding sales of shoes to your company (REDACTED TEXT) for its employees.

You indicate that, REDACTED TEXT accrues and pays use tax on the portion of materials and supplies charged to overhead that is allocated to commercial contracts and government fixed-price contracts without progress payments clauses. From this phrase, I assume that REDACTED TEXT purchases these materials and supplies ex-tax for resale and accrues use tax on the materials and supplies it consumes in performing these contracts. You describe the purchase of the shoes as follows:

"A defense contractor (presumably REDACTED TEXT) allows a vendor, that sells safety shoes, to sell its product on the contractor's premises on a periodic basis. Defense contractor employees obtain shoes and wear them in performing their duties while working the defense contractor. That safety shoe vendor bills the defense contractor for the entire cost of the shoes. The defense contractor pays the safety shoe vendor. Employee's that are required to have safety shoes and obtain the shoes are given an allowance. The defense contractor withholds the employee's portion of the cost of the shoes from their pay. The contractor's portion of the cost of the shoes is charged to an overhead account that is allocated to all contracts."

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 noted, all statutory references are to the Revenue and Taxation Code.) A "retail sale" means a sale for any purpose other than resale in the regular course of business in the form of tangible personal property. (§ 6007.)

"It 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.) The retailer owes the sales tax, but may collect sales tax reimbursement from the purchaser pursuant to agreement. (Civ. Code § 1656.1.)

B. Tax Consequences to REDACTED TEXT.

As you describe it, these sales appear to be to REDACTED TEXT for its own consumption. The fact that the workers who ultimately receive these shoes reimburse REDACTED TEXT for a part of its cost does not, by itself, create resales of the shoes to the workers. REDACTED TEXT is, then, the consumer of the shoes. As a result, the supplier owes sales tax on these sales and may collect sales tax reimbursement from REDACTED TEXT.

The facts indicate that some of REDACTED TEXT's contracts have progress payments clauses while some do not. Under the Aerospace rule, those clauses transform sales of overhead materials to a government contractor from taxable retail sales to ex-tax sales for resale to the United States. REDACTED TEXT may purchase for resale only the shoes which are allocated to government contracts containing progress payments clauses. Assuming that some of these purchases are for resale to the United States and some are not, REDACTED TEXT may buy all of the shoes free of tax for resale and report and pay use tax on those purchases which were allocated either to private commercial contracts or government contracts which do not contain progress payments clauses. The measure of tax is the entire cost of the shoes to REDACTED TEXT. Since REDACTED TEXT is the consumer, no deduction for the portion paid by the employees is available.

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

bc: San Jose District Administrator