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STATE OF CALIFORNIA

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January 18, 1994

Mr. R. K---  
R--- E---, Inc.  
P. O. Box XXXX  
---, CA XXXXX-XXXX

Dear Mr. K---:

This is in response to your letter dated November 15, 1993 in which you ask how tax applies to U.S. Government contracts. You state:

“R--- E--- is a ‘Time and Material’ sub-contractor to E--- E---, XXXX --- ---, [City], NC XXXXX. E---’s contract with the Department of Defense is to furnish a fully installed ‘Uninterruptible Power Supply System’ at the --- Air Force Base in [City], CA. The ‘U.P.S.’ system backups generators that provide electrical power for the Military Base operations.

“E--- is furnishing the batteries and other major components for the system. R--- E--- is furnishing the electrical labor and materials necessary for the assembly and installation. The bulk of the materials furnished by R--- E--- will be conduit and wire. All materials are purchased directly and shipped to the project. They are not used for any other purpose by either R--- or E--- before title is passed to the Government.”

You ask two questions:

“Does an ‘Uninterruptible Power Supply System’ fit into the sales tax code’s definition of ‘Machinery and Equipment’? As generator’s do it appears reasonable to assume that the U.P.S. system would.

“If the U.P.S. system does fit the ‘Machinery and Equipment’ definition, does sales tax apply to the purchase of sales of ‘Materials’ for this project. If not, R--- would issue a ‘Resale Certificate’ to all of its vendors.”

A “construction contract” means and includes a contract to erect, construct, alter, or repair any building or other structure, development, project, or other improvement on or to real property. (Reg. 1521(a)(1)(A)(1).)

A “United States construction contractor” means and includes a construction contractor, including a sub-contractor, who for itself, in conjunction with or by or through others, agrees to perform and does perform a construction contract for the United States Government. (Reg. 1521(a)(1)(B).)

The tax treatment in regard to tangible personal property furnished to the United States by contractors is set forth in Revenue and Taxation Code section 6007.5 which states that a sale of tangible personal property to a contractor for use in the performance of a contract for construction of improvements on or to real property in this State is a retail sale. The gross receipts from such a sale or the sales price of the property sold shall be included in the measure of tax. This is explained in subdivision (b)(1)(A) of Regulation 1521, which states that United States construction contractors are considered the consumers of materials and fixtures, and sales tax applies to the purchase by the contractor of those materials or fixtures. (See also Rev. & Tax. Code § 6384.)

Construction contractors are sellers of machinery and equipment furnished to the United States Government in connection with the performance of a construction contract. As the retailer, the contractor is entitled to purchase that machinery or equipment extax by issuing a resale certificate to its vendors. (Reg. 1521(b)(1)(B).)

“Machinery and equipment” is defined as property intended to be used in the production, manufacturing, or processing of tangible personal property, the performance of services, or for other purposes not essential to the fixed works, building, or structure itself, but which property incidentally may, on account of its nature, be attached to the realty without losing its identity as a particular piece of machinery or equipment and, if attached, is readily removable without damage to the unit or to the realty. (Reg. 1521(a)(6).) Appendix C of Regulation 1521, which is a list of items typically regarded as machinery and equipment, includes unaffixed electric generators, or, if affixed, generators which meet the requirements of subdivision (a)(6) of Regulation 1521. For purposes of this analysis, a U.P.S. is equivalent to a generator. Here the U.P.S. appears to be essential to the real property as opposed to being used, for example, in a manufacturing process. As such, it does not constitute machinery and equipment under subdivision (a)(6) of Regulation 1521.

“Fixtures” includes items which are accessory to the building or other structure and do not lose their identity as accessories when installed. (Reg. 1521(a)(5).) For instance, electric generators affixed to and accessory to a building, structure or fixed works are regarded as fixtures. (Appendix B of Regulation 1521.)

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The Court in Crocker National Bank v. City and County of San Francisco (1989) 49 Cal.3d 881 set out criteria for defining fixtures. One criteria it used was the adaptability to the use and purpose for which the realty is used. In the R--- contract the U.P.S. system, which is being installed at a military installation, acts as a backup for generators that provide electrical power to the military base and is an aid in making that real estate more suitable for its use as a military installation. Another criteria the Crocker Court used was the intention with which the annexation is made. Based on the nature of the U.P.S., a backup to the power supply source, it is our opinion the U.P.S. is placed on the property with the intent that it become a permanent part of the real estate. Thus, we conclude the U.P.S. is a fixture and not machinery and equipment.

The remaining question is whether the conduit and wiring are fixtures or materials. "Materials" include property (among other things, conduit and wiring) incorporated into real property which loses its identity and becomes an integral and inseparable part of the real property. (Reg. 1521(a)(4).)

If the conduit and wiring are incorporated as part of the U.P.S. in such a way that they become an integral part of the U.P.S., they take on the same characteristic, i.e., fixtures, otherwise they are considered materials. In either case, R--- E--- is considered the consumer of the conduit and wiring as well as the fixtures (the U.P.S.) and as such, the sale to R--- [E---] or its use of such property is subject to tax.

If we can be of further assistance please feel free to write again.

Sincerely,

Rachel M. Aragon  
Staff Counsel

RMA:ljt

cc: --- --- - District Administrator (--)