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STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

450 N STREET, SACRAMENTO, CALIFORNIA
(P.O. BOX 942879, SACRAMENTO, CALIFORNIA 94279-0001)
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Third District, San Diego

MATTHEW K. FONG
Fourth District, Los Angeles

GRAY DAVIS
Controller, Sacramento

CINDY RAMBO
Executive Director

October 31, 1991

Dear REDACTED TEXT,

Enclosed is a copy of the Decision and Recommendation pertaining to the petition for redetermination in the above-referenced matter.

I have recommended that the determination be redetermined in accordance with the reaudit as explained in the Decision and Recommendation.

There are three options available to you at this point.

1. If, after reading the Decision and Recommendation, you believe that you have new evidence and/or contentions, you should file a Request for Reconsideration. No special form is required to file the Request for Reconsideration, but it must be filed within 30 days from the date of this letter and clearly set forth any new contentions. If new evidence is the basis for filing the request, the evidence must be included. Direct any such request directly to me, with a copy sent to the State Board of Equalization, P.O. Box 942879, Sacramento, CA 94279-0001, Attn: Principal Tax Auditor. I will subsequently notify you whether the request has been taken under review or whether the request is insufficient to warrant an adjustment. If I conclude that no adjustment is warranted, I will then notify you of the procedure you can follow to request an oral hearing before the Board.

2. If, after reading the Decision and Recommendation, you find that there is no basis for filing a Request for Reconsideration, but nevertheless desire to have an oral hearing before the Board, a written request must be filed within 30 days with Ms. Janice Masterton, Assistant to the Executive Director, Board of Equalization, P.O. Box 942879, Sacramento, CA 94279-0001.

3. If neither a request for Board hearing nor a Request for Reconsideration is received within thirty (30) days from the date of this letter, the Decision and Recommendation will be presented to the Board for final consideration and action.

Very truly yours,

Susan W. Wengel
Staff Counsel

SMW:te
Enc.

cc: Ms. Janice Masterton
Assistant to the Executive Director (w/enclosure)

Mr. Glenn Bystrom
Principal Tax Auditor (file attached)

Oakland – District Administrator (w/enclosure)

Santa Rose – District Administrator (w/enclosure)

STATE OF CALIFORNIA
 BOARD OF EQUALIZATION
 BUSINESS TAXES APPEALS REVIEW SECTION

In the Matter of the petition)
 for Redetermination Under the) DECISION AND RECOMMENDATION
 Sales and Use Tax Law of:)
)
)
)
Petitioner)

The above-referenced matter came on regularly for hearing before Reviewing Attorney Susan M. Wengel on August 28, 1991, in Oakland, California.

Appearing for Petitioner: REDACTED TEXT

Appearing for the
 Sales and Use Tax Department: Helen Stratton
 Senior Tax Auditor

Protested Item

The protested tax liability for the period October 1, 1986 through September 30, 1988 is measured by:

<u>Item</u>	<u>State, Local and County</u>
B. Claimed sales for resale not supported by resale certificates	\$5,032,932
Reaudit adjustment	- <u>212,320</u>
Measure per reaudit	\$4,820,612

Contentions of Petitioner

1. The turbines and generators should be classified as machinery and equipment.
2. In the alternative, if the turbines and generators are classified as fixtures, REDACTED TEXT should be the party responsible for the tax.

Summary of Petition

Petitioner was a corporation which manufactured and sold diesel engine generators and related products. Petitioner ceased operations in 1988. The Sales and Use Tax Department (Department) audited petitioner's records and found that petitioner had entered into a contract with REDACTED TEXT to provide five 3,000 kw gas turbine generators and associated support equipment. REDACTED TEXT was the prime contractor for the U.S. Department of the Army for the construction of the Shuttle Transport System power plant at Vandenberg Air Force Base. Petitioner did not receive a resale certificate from REDACTED TEXT.

The specifications set out by REDACTED TEXT for the generators required that the engines be removable and that the components be mounted on a common skid. (See Exhibit A attached.) The generators were delivered to the job site or to a designated storage area by petitioner. REDACTED TEXT then placed the skids on a cement pad and built a casing around the generators which had walls that were easily disassembled for major overhauls and removal. The housing for the generators had a trolley and a hoist over the turbines so that they could be lifted for servicing.

The Department concluded that because the turbines and generators are so large, are housed in a separate structure, and are an integral component of the launch platform's electrical system, the generators are properly classified as fixtures. A sales tax was assessed when it was concluded that petitioner was not making sales of fixtures for resale.

Petitioner contends that the generators are machinery or equipment because the function of the generators was to provide electrical power for testing and experimentation on the space shuttle system. Petitioner's treasurer, REDACTED TEXT, testified at the appeal hearing that the generators were installed because the Army did not want to have to rely on the public power system during a launch. Although the generators appear to never have been used due to cutbacks in the space shuttle program, the generators were to be used during the launch to assure that there would be no loss of power. Kennedy Space Center uses an auxiliary power source during a launch and a similar system was to be used at Vandenberg during all its shuttle launches. There is no evidence that the generators have replaced the normal electrical system at the launch site or that they have been hooked up to operate in coordination with the normal system. The generators also do not appear to have been moved or put to any other use on the base.

Analysis and Conclusion

Sales and Use Tax Regulation 1521(a)(1)(A) defines a construction contract as a contract, whether on a lump sum, time and material, cost plus, or other basis, to erect, construct, alter, or repair any building or other structure, project, development, or other improvement on or to real property. It does not include a contract for the sale and installation of tangible personal property such as machinery and equipment. (Regulation 1521(a)(1)(8)(1).)

The term "construction contractor" means any person who for himself, in conjunction with, or by or through others, agrees to perform and does perform a construction contract. (Regulation 1521(a)(2).)

Regulation 1521(a)(5) and (6) further provide:

"(5) 'Fixtures' means and includes items which are accessory to a building or other structure and do not lose their identity as accessories when installed.

"(6) 'Machinery and equipment' means and includes property intended to be used in the production, manufacturing or processing of tangible personal property, the performance of services or for other purposes (e.g., research, testing, experimentation) 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. 'Machinery and equipment' does not include junction boxes, switches, conduit and wiring, or valves, pipes, and tubing incorporated into fixed works, buildings, or other structures, whether or not such items are used solely or partially in connection with the operation of machinery and equipment, nor does it include items of tangible personal property such as power shovels, cranes, trucks, and hand or power tools used to perform the construction contract."

The facts show that petitioner's contract with REDACTED TEXT was to merely furnish the generators. Petitioner was not responsible for the installation. Petitioner, therefore, is not a construction contractor but merely a retailer of generators. (Compare Hayward Bldg. Co. v. State Board of Equal. (1958) 164 Cal.App.2d 607, with Western Concrete Structures, Inc. v. State Bd. of Equalization (1977) 66 Cal.App.3d 543.) REDACTED TEXT, however, is a construction contractor with a contract with the United States Army.

Sales and Use Tax Regulation 1521(b)(1)(A) provides that 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. If the generators are fixtures, petitioner's sale to REDACTED TEXT will be taxable because as a consumer of all fixtures, REDACTED TEXT cannot be considered to be reselling the generator to the United States Army. Petitioner, not REDACTED TEXT will be the party responsible for the tax if the generators are fixtures.

Regulation 1521(b)(1)(8) provides that United States construction contractors are retailers of machinery and equipment they furnish in performing construction contracts with the United States Government. If the generators are found to be machinery and equipment, therefore, the sale to REDACTED TEXT would be a sale for resale.

The generators in question are skid mounted and are bolted to the floor of the specially made building so that within two days the unit can be detached from the building and removed with a crane. Petitioner contends that because the generators are easily removed they are not fixtures.

In the case of C. R. Fedrick v. State Board of Equalization (1988) 204 Cal.App.3d 252, the court addressed a similar issue. The Fedrick court applied case law and Regulation 1521 and concluded that certain compressors which were bolted to concrete foundations were fixtures. The court concluded that the fact that components could be easily disassembled and removed did not

alone establish their character as personality. Consideration was given to the fact that even though the components could be moved, they were not actually relocated often.

In the present appeal, the generators have not been moved or even used in any manner. Their mobility seems to have been created basically for ease in maintenance. The generators, like the components in the Fedrick case, were constructed so as to adapt to the use and purpose of the realty. The generators were housed in a building which could withstand the heat of a launch and they were designed to provide the power for the launch site during a lift-off. This does not lead to the conclusion that the generators were used for testing purposes only. Once operational, the generators were to become the source of electrical power for the entire launch site during all launches and were necessary to the realty.

It must be concluded that the generators are fixtures and that the sale to REDACTED TEXT is a taxable sale for which petitioner and not REDACTED TEXT is responsible for the tax.

It is noted that if petitioner wishes to submit evidence that the selling price is incorrect or that a bad debt deduction is appropriate, a request for reconsideration may be made along with evidence supporting the adjustment.

Recommendation

It is recommended that the tax liability be redetermined in accordance with the reaudit dated June 6, 1990.

Susan M. Wengel, Staff Counsel

Sept. 18, 1991