

CALIFORNIA STATE BOARD OF EQUALIZATION
APPEALS DIVISION BOARD HEARING SUMMARY

In the Matter of the Petition for Redetermination)
Under the Sales and Use Tax Law of:)
BAY AREA HIGH REACH, INC.) Account Number SR CH 97-201043
Petitioner) Case ID 374287
Hayward, Alameda County

Type of Business: Lessor and retailer of scaffolding equipment

Audit period: 04/01/02 – 03/31/05

<u>Item</u>	<u>Disputed Amount</u>
Unreported lease receipts	\$5,605,260
Tax as determined and protested	\$470,359.76
Interest through 09/30/13	<u>370,410.71</u>
Total tax and interest	\$840,770.47
Payments	<u>- 1,501.29</u>
Balance Due	<u>\$839,269.18</u>
Monthly interest beginning 10/01/13	<u>\$ 2,344.29</u>

This matter was scheduled for Board hearing in March 2009, but was postponed for settlement consideration. It was rescheduled for hearing in January 2013 but was deferred at the request of the Appeals Division in order to issue a second supplemental D&R.

UNRESOLVED ISSUE

Issue: Whether adjustments are warranted to the amount of unreported lease receipts. We find no adjustment is warranted.

Petitioner leases scaffolding to its customers for use at construction sites. During the audit period, petitioner's contracts with its customers included the furnishing, erecting, and dismantling of scaffolding for a set all-inclusive price. The contracts also provided for an additional rental charge if the scaffolding remained in the air longer than the number of days established in the contract. Petitioner leased the scaffolding in substantially the same form as it was acquired, and petitioner paid tax reimbursement to its vendor with respect to some of its purchases of scaffolding.

1 The Sales and Use Tax Department (Department) found that petitioner purchased the majority
2 of the scaffolding ex tax (without payment of sales tax reimbursement to the vendor or payment of tax
3 on returns). Since scaffolding consists mainly of planks of wood and metal rods that are virtually
4 indistinguishable from one another once placed in inventory, the Department computed percentages of
5 scaffolding purchased ex tax each quarter, which ranged from 75 to 85 percent. The Department
6 applied those percentages to petitioner's lease receipts to establish the lease receipts subject to tax.

7 Petitioner contends that the amount subject to tax should not include labor charges, arguing that
8 its lease agreements are more like service agreements than leases of tangible personal property. In
9 order to illustrate its argument, petitioner submitted a Proposal and Acceptance form (proposal) along
10 with an Estimator Worksheet (worksheet) which it uses to determine the amount to charge its customer
11 for the lease. The worksheet shows 41 man hours required for the job it represents, with a total amount
12 charged for labor of \$4,100; it also shows a \$17 per day rental fee for days in addition to the number of
13 days established in the contract. Petitioner asserts that the contracts were essentially contracts for
14 nontaxable labor, and argues that the charges for labor should be removed from the audited measure of
15 tax. Alternatively, petitioner contends that its tax liability should be limited to tax on the cost of its
16 purchases of scaffolding, since it intended to pay tax on those purchases when the scaffolding was
17 acquired, believed it was paying tax, and would have made a timely election to pay tax if it had been
18 aware that it was not paying sales tax reimbursement to its vendor.

19 The transactions at issue are leases because petitioner temporarily transferred possession and
20 control of tangible personal property (scaffolding materials) for consideration. It is undisputed that
21 petitioner did not pay tax reimbursement to its vendors on most of its purchases of scaffolding, or
22 make a timely election to report tax. Thus, the lease receipts are subject to tax (Cal. Code Regs., tit.
23 18, § 1660, subd. (c).) The regulation expressly prevents petitioner from making an untimely election
24 to report tax (Cal. Code Regs., tit. 18, § 1660, subd. (c)(3).) Therefore, we reject petitioner's
25 contention that its tax liability should be limited to tax on the cost of its purchases of scaffolding based
26 on its expressed intent to pay tax reimbursement to its vendor or on its statement that it would have
27 made a timely election to pay tax when the scaffolding was first leased had it been aware tax
28 reimbursement had not been paid to the vendor.

1 We now address petitioner's primary contention, that there should be an adjustment for the
2 amount of labor charges included. First, we find that the services provided by petitioner are
3 mandatory, because the proposal petitioner provides to its customers contains the following language:
4 "Per OSHA Regulations, no alterations or dismantling can be done by any contractor or agent (only by
5 Bay Area High Reach, Inc.). Any alterations by the contractor (lessee) or their subcontractors will
6 void any indemnity agreements." Since the customer does not have an option to dismantle, move,
7 and/or re-erect the scaffolding, or to have someone other than petitioner perform those tasks, we
8 conclude the services petitioner provided were part of the continuing sale and purchase (i.e., lease) of
9 the scaffolding, and therefore are subject to use tax. (Rev. & Tax. Code, § 6011, subds. (a)(2), (b)(1).)
10 With respect to petitioner's assertion that the substance of the transactions was the provision of
11 services, we need to determine whether the true object of the contracts is the service or the tangible
12 personal property that is transferred. We find that the true object sought by petitioner's customers was
13 the actual end product, the scaffolding itself, which allowed petitioner's customers to perform
14 construction work on various projects that would not have been possible without the scaffolding.
15 Accordingly, the contracts were leases of tangible personal property, with services included as part of
16 the leases, and petitioner's rental receipts are subject to tax.

17 In the D&R, we recommended, however, that the Department conduct a reaudit to determine if
18 any portion of the lease receipts represented nontaxable charges for installation labor. In its post-D&R
19 review, the Department concluded that there is insufficient evidence to show that any portion of the
20 labor represented installation labor. In the SD&R, we note that petitioner does use the term
21 "installation" on its estimator worksheet. However, petitioner has used the terms "install" and "erect"
22 interchangeably. We find that petitioner fabricates temporary, free-standing structures, which are not
23 attached to realty, by assembling together at the jobsite the raw materials it delivered to the jobsite,
24 including wooden planks and metal rods, piece by piece. As a result we conclude that any potential
25 installation labor (i.e., affixing the scaffolds to realty) would be *de minimis*. Further, we find petitioner
26 has not shown that any portion if its charges for labor represent nontaxable charges for installation
27 labor. Accordingly, we recommend no adjustment.

RESOLVED ISSUE

1
2 Since petitioner did not participate in the amnesty program, an amnesty interest penalty of
3 \$11,788.03 will be added when the liability becomes final. Petitioner has requested relief of the
4 amnesty interest penalty on the basis that, prior to March 31, 2005, the deadline for filing for amnesty,
5 it was unaware of any outstanding tax liability.

6 Petitioner first received notice of the upcoming audit on June 16, 2005, after the deadline for
7 filing for amnesty. Further, we find that petitioner believed in good faith that it had paid tax on its
8 purchases of scaffolding, and, as a result believed that its leases were not subject to tax. Thus, we find
9 that, prior to the deadline for filing for amnesty, petitioner was unaware that it had additional tax
10 liability for the amnesty-eligible period. Therefore, we recommend relief of the amnesty interest
11 penalty if, within 30 days of the Notice of Redetermination, petitioner either pays in full the amnesty-
12 eligible tax and interest due or enters into an installment plan to do so within 13 months and
13 successfully completes that agreement.

OTHER MATTERS

14
15 None.

16
17 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III
18
19
20
21
22
23
24
25
26
27
28