



1 purchased without payment of tax or tax reimbursement, either by furnishing resale certificates or  
2 making purchases from out-of-state vendors. A small portion of petitioner's sales were over-the-  
3 counter sales (wall-bed kits without installation) that included retail sales, nontaxable sales for resale,  
4 and exempt sales in interstate commerce. For its lump sum construction contracts, petitioner  
5 separately recorded its material costs, offsite labor costs, and jobsite labor costs. Petitioner did not  
6 allocate the jobsite labor costs between on-site assembly labor and on-site labor to affix the units to the  
7 wall. Before the first quarter 2006 (1Q06), petitioner reported its sales as if all contracts (whether they  
8 included installation or not) were tax-included. Petitioner then computed its deductions for sales tax  
9 included. For wall-bed kits that were not installed, petitioner computed the amount of tax using the  
10 tax rate and the total amount charged to customers. For its installed wall-bed sales, petitioner  
11 subtracted all labor charges for jobsite labor and computed the amount of tax included in the remainder  
12 (which represented materials and offsite labor). Beginning 1Q06, petitioner stopped reporting its lump  
13 sum contracts as total sales and instead began reporting the cost of materials installed pursuant to lump  
14 sum contracts as purchases subject to use tax (it made no changes to its method of reporting over-the-  
15 counter sales of wall-bed kits).

16 The Sales and Use Tax Department (Department) found that petitioner's wall-bed units are not  
17 typical "Murphy" wall beds, which are ordinarily treated as fixtures for sales and use tax purposes,  
18 because the bed frames on petitioner's units could not easily be removed or replaced once constructed.  
19 Instead, the Department concluded that the wall-beds and matching cabinetry installed by petitioner  
20 were fixtures only if they were prefabricated (i.e., 10 percent or less of the total direct costs were  
21 incurred to install the unit). To determine which of the wall-bed units installed by petitioner were  
22 fixtures, the Department scheduled the direct material and labor costs of each lump sum contract using  
23 petitioner's own records. Since petitioner did not separately record assembly labor and installation  
24 labor at the jobsite, based on its discussions with petitioner, the Department considered 50 percent of  
25 the jobsite labor cost to represent labor to affix the assembled unit to the wall.<sup>3</sup> Using that estimate,

---

26  
27 <sup>3</sup> Petitioner originally estimated that 25 percent of the jobsite labor cost represented installation labor and later revised that  
28 estimate to 75 percent. However, petitioner did not provide evidence to support the increase in its estimate. Based on the  
Department's understanding of the installation process, as well as the instruction sheets included with wall-bed kits, the

1 the Department computed the amount of installation labor for each of petitioner's lump sum contracts  
2 and found that all but two of the units were fixtures because they were prefabricated wall-bed/cabinet  
3 units. Petitioner had reported tax on the cost of materials rather than on the sale of fixtures. The  
4 Department calculated that the difference between the measure petitioner should have reported on the  
5 sale of the fixtures compared to the cost it actually reported on cost is \$59,079. The Department also  
6 found that petitioner had erroneously claimed \$11,125 of taxable assembly labor as nontaxable  
7 installation labor prior to 1Q06.

8         Petitioner contends that there was no understatement of taxable measure related to installed  
9 wall beds and that all claimed nontaxable labor represented installation labor. Petitioner states that,  
10 beginning in 2006, it determined (based on a review of Board publications and discussions with Board  
11 staff) that its wall-beds were not fixtures, but were materials that became a permanent part of the real  
12 estate when affixed to the wall. Petitioner claims that the units cannot be removed without destroying  
13 the unit and the wall where it is affixed. Petitioner further asserts that the jobsite assembly labor is  
14 either part of the nontaxable installation labor, or minimal compared to the total jobsite labor, because  
15 the wall-bed and cabinet units are large, heavy, and installed on walls that sometimes are not straight,  
16 thus requiring time-intensive finish work.

17         In general, construction contractors are consumers of the materials and retailers of the fixtures  
18 they furnish and install in the performance of construction contracts. (Cal. Code Regs., tit. 18, § 1521.)  
19 "Materials" means and includes construction materials and other tangible personal property  
20 incorporated into, attached to, or affixed to real property which loses its identity to become an integral  
21 and inseparable part of the real property. (Cal. Code Regs., tit. 18, § 1521., subd. (a)(4).) "Fixtures"  
22 means and includes items which are accessory to a building or other structure, and which do not lose  
23 their identity as accessories when installed. (Cal. Code Regs., tit. 18, § 1521, subd. (a)(5).) One  
24 example of a fixture is a prefabricated cabinet. (Cal. Code of Regs., tit. 18, § 1521, Appendix B.) A  
25

---

26 Department concluded that the actual percentage of installation labor to total jobsite labor was closer to 25 percent than  
27 75 percent. Nevertheless, to give petitioner the benefit of the doubt, the Department used an estimate of 50 percent (the  
28 larger the percentage of installation labor, the less likely the item would have constituted a fixture, which in turn would  
result in a lower tax liability).

1 cabinet is considered prefabricated and a fixture when 90 percent of the total direct labor and material  
2 cost to fabricate and install the cabinet is incurred before the contractor affixes the cabinet to the realty.  
3 (Cal. Code Regs., tit. 18, § 1521, subd. (c)(2).) Jobsite fabrication labor includes assembly labor  
4 performed prior to attachment of a component of a fixture to a structure or other real property. (Cal.  
5 Code Regs., tit. 18, § 1521, subd. (b)(2)(B)(2).)

6         The wall-bed units here are essentially cabinets that contain a structure that can support a  
7 mattress. Further, while the wall-bed units may be considered permanent since they are impossible to  
8 remove without some damage to the unit or wall, the units are not necessary to the integrity of the  
9 structure and do not lose their identity after they are assembled and attached to the wall. Accordingly,  
10 we consider the wall-beds and matching cabinetry at issue to be cabinets. Since the subject wall-bed  
11 units were not fully assembled prior to their delivery to the job-site, we must determine whether the  
12 units qualify as prefabricated cabinets, which are considered fixtures. Petitioner's description and  
13 photographs of the wall-units evidence large units, with multiple cabinets, that would require  
14 significant assembly labor. Petitioner's installation instructions show that the first eight of the ten  
15 steps in the installation instructions are for pre-installation assembly, and actual installation is  
16 performed only in the final two steps. Thus, these instructions show that a substantial percentage of  
17 the jobsite labor involves assembly rather than affixation. We conclude that the Department's  
18 allocation of 50 percent of the jobsite labor as installation labor is reasonable, if not generous. When  
19 the audited cost of on-site assembly labor is added to the off-site assembly labor, the total results in at  
20 least 90 percent of the direct cost of labor and material to fabricate and install the majority of the wall-  
21 beds. Thus, we find that the Department has correctly regarded the pre-fabricated wall-bed units as  
22 fixtures, and we recommend no adjustments to the underreported wall-bed sales or the disallowed  
23 claimed nontaxable labor.

24         **Issue 2:** Whether adjustments are warranted to the disallowed claimed deductions for sales tax  
25 included. We recommend no adjustment.

26         This issue relates to petitioner's sales of wall-bed kits, without installation. Although the  
27 contracts for those sales did not indicate whether sales tax reimbursement was included in the contract  
28 price, petitioner claimed deductions on its returns totaling \$2,774. The Department found that there

1 was insufficient evidence to conclude that the contract prices for wall-bed kits included sales tax  
2 reimbursement, and therefore disallowed the claimed deductions. Petitioner contends that its sales of  
3 wall-bed kits did include tax and asserts that it told customers the contract price included sales tax  
4 reimbursement.

5 In addition to noting that the sales contracts do not indicate that sales tax was included, the  
6 Department visited petitioner's business location and did not see any written notices, in any form,  
7 indicating that petitioner included sales tax reimbursement in the total price of wall-bed kits. Also,  
8 petitioner did not furnish any documents (price tags, advertisements, etc.) or customer witnesses to  
9 support its claim that the selling prices included tax reimbursement. Therefore, we find the evidence  
10 does not support a finding that petitioner's contract prices for wall-bed kits included tax  
11 reimbursement, and we recommend no adjustment to the disallowed claimed deductions for sales tax  
12 included.

13 **OTHER DEVELOPMENTS**

14 None.

15  
16 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28