

9-26-86

330.3970

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

In the Matter of the Petition)
for Redetermination Under the)
Sales and Use Tax Law of:)

DECISION AND RECOMMENDATION

[Redacted])
([Redacted])
Taxpayer)

The preliminary hearing on the above taxpayer's petition for redetermination was held on January 6, 1986, in Fresno, California.

Hearing Officer:

Warren W. Mangels

Appearing for Petitioner:

Mr. [Redacted]
Attorney at Law

Mr. [Redacted]
Vice President/Secretary

Appearing for the Board:

Ms. Linda Alexander
Auditor

Mr. Anthony Costa
District Principal Auditor

Mr. E. J. Snortland
Supervising Tax Auditor

(This preliminary hearing was held the same time as the preliminary hearing concerning the claim for refund of the partnership of [Redacted] and [Redacted])

[Redacted] [SR DH 22], involving similar issues]. Therefore, this hearing report is a companion one to the report concerning that predecessor's claim for refund, and is to be read with that report. The predecessor will be referred to as "Partnership", this taxpayer as "Corporation".)

Protested Items

Corporation filed a petition for redetermination, dated March 18, 1985, concerning a tax deficiency determination, issued February 15, 1985, for the period October 1, 1982 through June 30, 1984. A claim for refund for that period was also duly filed concerning Item B, below. There is also a supplemental brief dated January 15, 1986. The protest involves tax determined on the following audit items:

<u>Item</u>	<u>State, Local and County</u>
A. Erection labor disallowed	\$208,921
B. Less: "Tax-paid" purchase credit not claimed	-138,103
Net amount protested	\$ 70,818

Contentions of Corporation

1. The "post-and-fabric" fence rentals do not constitute sales because they were leases of tangible personal property in substantially the same form as acquired by Corporation as to which Corporation paid sales tax reimbursement measured by the purchase price of the property.

2. The charges for removing the rented "panel fencing" are not taxable; moreover, if the "post-and-fabric" fencing rentals are determined to constitute taxable sales, in the alternative the charges for removal of that fencing also are not taxable.

3. The charges for installing the rented "panel fencing" are not taxable; moreover, if the "post-and-fabric" rentals are determined to constitute taxable sales, in the alternative, the charges for installation of that fencing are also not taxable.

4. The charges for damaged returned merchandise are not taxable.

5. In the alternative, the doctrine of equitable estoppel should apply to result in nontaxability of the "erection labor" charges."

Summary of Facts

During the period July 1, 1981 through September 30, 1982, the predecessor partnership (hereinafter "Partnership"), the subject of the companion preliminary hearing report, was engaged in the business of leasing portable fences. It also made retail sales of accessories for fences, such as chains and locks. Partnership filed a claim for refund for that period. Partnership commenced operating in January of 1980. Consequently, there was no prior audit of either entity.

In September of 1982, this petitioner-corporation, hereinafter "Corporation", acquired the assets of Partnership in a transaction exempt from tax as an occasional sale. (Sections 6006.5(b) and 6367 of the Revenue and Taxation Code.)

Thereafter, Corporation continued to engage in the identical operations as those previously conducted by Partnership.

Their rental operations consisted of renting two types of portable fencing: (1) "panel" fencing; and (2) "post-and-fabric" fencing."

Panel Fencing Rentals

This involves their first acquiring fencing materials in the form of separate pipes and separate rolls of fabric (chainlink) materials both "tax-paid" and then constructing therefrom fabricated chainlink fence panels. Each panel is constructed at the location of Partnership and Corporation by building a frame of the piping around the fabric material, and permanently attaching the fabric to that frame. An inventory is kept of the individual completed panels.

When a contract is made for temporary panel fencing, the individual panels required are transported to the jobsite. At the jobsite, the panels are assembled and erected by the taxpayers by being tied together, and are placed in the proper position as designated by the lessee.

The assembled and erected panel fencing that is temporarily rented to the customers retains its status as tangible personal property while in the possession of the lessee. To the extent that there is any actual affixation to realty, such affixation is only temporary.

Normally, the rental agreement provides for (1) a basic monthly rental charge, (2) a separate charge for delivery, and (3) an additional separate charge for the labor involved at the jobsite to assemble the panels together and attach them to the ground and for the labor to ultimately remove them upon termination of the lease. This third charge (for assembly, attachment, and removal) is a combined charge.

Copies of sample written lease agreements and sample sales invoices concerning panel fencing rentals during the audit period are attached to this preliminary hearing report as Exhibits A through D.

Taxpayer did not regard the above jobsite labor charge (3) as taxable. The district office staff concluded that the charge was for taxable fabrication and assembly labor, and for a service that was part of the sale, pursuant to the provisions of section 6011 of the Revenue and Taxation Code.

Post and Fabric Rentals

Again, the fence posts and rolls of fabric (chainlink material) are acquired "tax-paid". This portion of the inventory, however, unlike panel fencing, is kept at the taxpayers' location in the same form as acquired.

When a rental agreement for "post and fabric" fencing is made, the necessary rolls and posts are transported to the jobsite. The assembly, erection, and installation is accomplished by properly positioning the posts at the jobsite location in positions generally designated by the lessee, and affixing the fabric to the posts by tying the fabric to the posts. Ties, caps and rings are utilized and become components of the fencing.

The posts are sometimes pounded into fixed positions but because temporary use is involved, the affixation is generally not as extensive as in a construction contract.

At the end of the rental term, the fabric material is separated from the posts and returned to inventory by the taxpayers. The posts are also removed and returned to inventory.

Copies of sample audit period written rental agreements and sales invoices are attached to this preliminary hearing report as Exhibits E through H. As indicated in the Exhibits, normally post and fabric rental agreements provide

for an annual footage charge. Unlike panel fencing contracts, a "basic" rental charge is not normally separately stated.

Taxpayers do not regard the post and fabric rentals as sales. (See contention no. 1, above.)

The district office staff concluded that post and fabric fencing was not rented in substantially the same form as acquired, and, consequently, that the rentals constituted taxable sales by statutory definition. (Section 6006 (g)(5) of the Revenue and Taxation Code; see below.) A credit was given for "tax-paid" purchases.

Concerning panel fencing rentals (and also post-and-fabric fencing rentals, if they are determined to be sales) it is contended that dismantling and removal labor (i.e., the price factored into petitioner's labor charge that relates to the dismantling and removal of the tangible property from the lessee's real property) should be excluded from taxable gross receipts. It is also maintained that there should be an allowance for installation labor. No such allowances were made in the audit.

It is also urged that jobsite labor in the taxpayers' operations can be broken down for the audit period as follows:

Taxpayer Corporation, SR

Total labor	<u>\$209,921</u>	But see Item A amount)
A. "Post and fabric" labor	\$ 68,664	
B. "Panel" labor	<u>141,257</u>	
TOTAL	\$209,921	
A. Post and fabric labor - installation	\$ 34,332	
A. Post and fabric labor - removal	<u>34,332</u>	
A. Post and fabric labor - TOTAL	\$ 68,664	
B. Panel labor - installation	\$ 70,629	
B. Panel labor - removal	<u>70,629</u>	
B. Panel labor - TOTAL	\$141,258	

Taxpayer Partnership,

Total Labor	\$43,174	
A. Post and fabric labor		\$ 4,409
B. Panel labor		<u>38,765</u>
TOTAL		\$ 43,174
A. Post and fabric labor - installation		\$ 2,205
A. Post and fabric labor - removal		<u>2,204</u>
TOTAL		\$ 4,409
B. Panel labor - installation		\$ 19,383
B. Panel labor - removal		<u>19,382</u>
TOTAL		\$ 38,765

It is also asserted that some of the determined taxable gross receipts (Contention No. 4, above) concern nontaxable charges for damaged returned equipment. The amount claimed is \$6,222.61 with respect to "post and fabric" fencing with an additional amount claimed for "panel" fencing. Documentation submitted indicates "tax" was charged on at least some of these damaged returns.

It is also maintained (concerning Contention No. 5, above) that [redacted] visited the Fresno Board office and requested advice with respect to computing sales tax liability on the rental operation; that they were informed verbally that sales tax was not, in any way, computed with respect to any labor to install or remove; and that taxpayers consequently structured their bidding and cost and profit structures accordingly. Taxpayer therefore maintains that the equitable theory of estoppel should apply to this case, insofar as the separately stated labor charges are concerned.

Analysis and Conclusions

The first issue presented is whether the post and fabric fence rentals constitute sales.

Pursuant to the relevant parts of section 6006 (g)(5) of the Revenue and Taxation Code, any lease of tangible personal property for a consideration except a lease of tangible personal property leased in substantially the same

form as acquired as to which the lessor has paid sales tax reimbursement or has timely paid use tax measured by the purchase price of the property is a sale.

For the following reasons, we conclude that the post and fabric fences under consideration here rented by taxpayers to the customers were leased to those customers in substantially the same form as acquired by the taxpayers; and that, consequently, the rentals did not constitute sales where the taxpayers paid sales tax reimbursement or timely paid use tax measured by the purchase price of the property, in view of section 6006 (g)(5) of the Revenue and Taxation Code.

That which was acquired by the lessees was essentially in the same form as initially acquired by the taxpayers, except that the property leased was installed by the taxpayers.

While there appears to have been an appreciable increase in value (and substantial cost to the taxpayers) occasioned by the labor performed by the taxpayers at the jobsite, a considerable portion of such increased value (and labor costs) was the result of installation labor, rather than fabrication labor.

It is true that one of the purposes in the statute of taxing rentals derived from tangible personal property no longer in substantially the same form after tax has been paid on the cost of its acquisition is to capture tax on the increased value resulting from the change in form. Here, however, rather than a substantial change in form of tangible personal property resulting from taxable fabrication labor, the increased value, in essence, was principally the result of performing nontaxable installation labor.

Therefore, subject to a limitation explained immediately below, the tax does not apply to the lease of the post and fabric fences.

We understand, however, with respect to some post and fabric transactions, taxpayers collected sales tax reimbursement. Section 6901.5 provides that if tax reimbursement is mistakenly computed upon an amount that is not taxable, the amount thereof shall be remitted to the state unless returned to the customer upon notification by the Board. Sales and Use Tax Regulation 1700, subdivision (b), provides, in pertinent part:

"(2) PROCEDURE UPON ASCERTAINMENT OF EXCESS TAX REIMBURSEMENT. Whenever the board ascertains that a person has collected excess tax reimbursement, the person will be afforded an opportunity to refund the excess collections to the customers from whom they were collected. In the event of failure or refusal of the person to make such refunds, the board will make a determination against the person for the amount of the excess tax reimbursement collected and not previously paid to the state, plus applicable interest and penalty.

"(3) EVIDENCE SUFFICIENT TO ESTABLISH THAT EXCESS AMOUNTS HAVE BEEN OR WILL BE RETURNED TO CUSTOMER.

"(A) If a person already has refunded to each customer amounts collected as reimbursement for tax in excess of the tax due, this may be evidenced by any type of record which can be verified by audit such as:

"1. Receipts or cancelled checks.

"2. Books of account showing that credit has been allowed the customer as an offset against an existing indebtedness owed by the customer to the person.

"(B) If a person has not already made sales tax reimbursement refunds to each customer but desires to do so rather than incur an obligation to the state, the person must:

"1. Inform in writing each customer from whom an excess amount was collected that the excess amount collected will be refunded to the customer or that, at the customer's option, the customer will be credited with such amount, and

"2. The person must obtain and retain for verification by the board an acknowledgement from the customer that the customer has received notice of the amount of indebtedness of the person to the customer.

"(4) OFFSETS. If a person who has collected excess tax reimbursement on a transaction fails or refuses to refund it to the customer from whom it was collected, the excess tax reimbursement shall be offset against any tax liability of the taxpayer on the same transaction. Any excess tax reimbursement remaining

after the offset must be refunded to the customer or paid to the state. The offset can be made when returns are filed, when a determination is issued, or when a refund is claimed. Such offsets can be made only on a transaction by transaction basis. Tax reimbursement collected on a specific transaction can be used only to satisfy a tax liability arising from the same transaction. The "same transaction" means all activities involved in the acquisition and disposition of the same property. The "same transaction" may involve several persons, such as a vendor, a subcontractor, a prime contractor, and the final customer; or a vendor, a lessor, and a series of sublessors. Tax reimbursement can be offset against the tax liability of the taxpayer whether the liability was satisfied by paying sales tax reimbursement to a vendor, paying use tax to a vendor, or paying use tax to the state.

"An offset of a taxpayer's own tax liability against tax reimbursement collected from a customer can be made only with respect to transactions in which possession of the property upon which the taxpayer's tax liability is based is transferred, either permanently or temporarily, to the customer, as in the case of construction contracts or leases....

"(5) PARTICULAR APPLICATIONS.

"(D) A lessor purchases property and pays sales tax reimbursement to the vendor. The property is leased in the same form as acquired and tax reimbursement is collected on the rental receipts. Tax reimbursement collected on rental receipts must be returned to the lessee or paid to the state to the extent that it exceeds the tax liability measured by the purchase price."

Concerning the "panel fencing", the issue is the taxability of the charges for labor at the jobsite. An analogy could be drawn to labor necessary to fabricate a massive table out of parts. The fact that some of the fabrication and assembly happened to occur at the location where the table is to be placed does not alter the circumstance that the labor constitutes the labor of producing the tangible personal property rented (sold), i.e., taxable fabrication labor required to produce the precise form of tangible personal property contracted for. Section 6011, subdivision (a)(2) of

the Revenue and Taxation Code provides, in pertinent part, that the taxable sales price means the total sale or rental price, without any deduction on account of the cost of the materials used, labor or service cost, or any other expense. Moreover, section 6011, subdivision (b)(1) thereof provides, in pertinent part, that the total amount of the sale or rental price includes any services that are a part of the sale.

On the other hand, section (c)(3) thereof does specifically exclude from the definition of taxable sales price the price received for labor or services used in installing or applying the property sold.

We have thoroughly reviewed the contention of the taxpayers with respect to panel fencing that all the jobsite labor constituted nontaxable installation labor and dismantling labor, the latter which is also asserted to be nontaxable. In applying the pertinent statutes, we do not agree with such contention for the following reasons:

As indicated by our analogy to a large table, because fabrication labor occurs at the jobsite does not detract from the fact that it is still fabrication labor. Fabrication of the panel fencing is completed at the jobsite, even though such fencing is also installed there.

It would appear, with respect to panel fencing, that 25 percent of the charge for jobsite labor would relate to nontaxable installation labor (i.e., attributable to discussions with the lessee concerning location, measuring for location, placement upon the specific location, etc.).

Charges allocable to the labor of dismantling and removal of the panel fencing are taxable. Dismantling and removal labor are performed in all of the taxpayer's rental contracts. Moreover, the charges therefor are not separately stated. They, therefore, constitute charges for taxable services that are part of the sale (rental) of the panel fencing.

Concerning the charges for damaged fencing, such charges appear not to represent taxable charges for rental (sale) of fencing but charges as compensation for damages.

Turning to the request for equitable relief under the application of the doctrine of equitable estoppel, there is no actual proof as to how the nature of the rental activity was described to the office representative.

In any event, taxpayers in essence are urging that because of advice given, the State of California should be estopped from denying a request for equitable relief. The Board lacks jurisdiction to exercise equitable powers. In addition, the doctrine of equitable estoppel is clearly inapplicable here. Where the sales or use tax liability of a taxpayer is involved, it has been held that estoppel will not lie against the state (Market Street Railway Co. v. State Board of Equalization, (1955) 137 Cal.App.2d 87 [290 P2d. 20]; see LaSociete Francaise v. California Employment Commission, (1943) 56 Cal.App.2d 534 [133 P2d. 47]).

It is to be noted that section 6596 of the Revenue and Taxation Code does provide statutory relief under certain very limited conditions, where it is clearly established that detriment has occurred as a consequence of the receipt of erroneous written advice. It provides in pertinent part:

"(a) If the board finds that a person's failure to make a timely return or payment is due to the person's reasonable reliance on written advice from the board, the person may be relieved of the taxes imposed by Sections 6051 and 6201 and any penalty or interest added thereto.

"(b) For the purposes of this section, a person's failure to make a timely return or payment shall be considered to be due to reasonable reliance on written advice from the board, only if the board finds that all of the following conditions are satisfied:

"(1) The person requested in writing that the board advise him or her whether a particular activity or transaction is subject to tax under this part. The specific facts and circumstances of the activity or transaction shall be fully described in the request.

"(2) The board responded in writing to the person regarding the written request for advice, stating whether or not the described activity or transaction is subject to tax, or stating the conditions under which the activity or transaction is subject to tax."

Taxpayers have obviously not met the statutory conditions required for providing that relief.

Recommendation

With respect to the claimant Partnership, [redacted], et al [redacted], the claim for refund should be allowed to the extent the measure reflects cost of materials purchased "tax-paid" which became components of subsequently rented (and consequently sold) panel fencing. Moreover, subject to limitations imposed by Section 6901.5, a refund should also be made of an amount necessary to treat the Partnership as a consumer of the rented post and fabric fencing, and, if warranted, subject to the same limitations, to adjust for nontaxable damage charges. Also with respect to leased panel fencing, an appropriate adjustment (25 percent) is to be made for a charge allocable to installation labor.

With respect to this petitioner Corporation (SR DH 22 010), the same appropriate adjustments are to be made.

Adjustments to be made by Fresno district office. No further adjustment.

Warren W. Mangels
Warren W. Mangels, Hearing Officer

9-26-86
Date

REVIEWED FOR AUDIT:

Principal Tax Auditor

Date