

_____ indicates that the federal government partially paid for building the _____, under a "Construction Differential Subsidy Program." While the subsidy was only allowed for the costs of property "delivered by the shipyards," _____ asserts that its purchase of the forklifts from the taxpayer also qualified for the program. The purchase subsidy was allegedly based on a finding of an unspecified government agency (apparently the Maritime Administration) that the forklifts were "capitalizable" as part of the vessel's construction cost. Some unidentified person or agency also classified the forklifts as "permanent," meaning that they are maintained on board as the primary cargo handling equipment. Because of these findings and classifications, if the _____ is ever "turned back" to the Maritime Administration, the forklifts must be turned in as a part of the vessel.

_____ has also submitted a letter from the United States Department of Commerce, Maritime Administration, discussing whether forklifts on Ro/Ro vessels qualify for a maintenance subsidy. The letter cites various provisions of General Order 20, presumably a rule or regulation of the Maritime Administration. The letter states that the subsidy is allowable only for "integral parts" of vessels, and that the term "vessel" includes "cargo handling equipment...intended for use primarily on the vessel." According to the letter, this "leads to the inference" that forklifts are integral parts of Ro/Ro vessels.

Your memo does not specify why exemption under Section 6368 was disallowed in the audit. Presumably, the audit found that the forklifts are not component parts of the _____ because they are not affixed or attached thereto in a substantial manner when in use. _____'s contentions on this point, and our responses, are as follows:

1. Citing dictionary definitions, _____ contends that the term "component" means "a constituent part," and further, that "constituent" means anything which "serves in making up a complete whole or unit; an essential part." _____ believes that the forklifts should be classified as component parts of the _____ because they are necessary and essential to the vessel's operation.

However, Sales and Use Tax Regulation 1594 contains its own definition of "component part" for purposes of Section 6368. Specifically, subdivision (c)(1) of the regulation provides in part:

"To be considered a 'component part' of a watercraft for purposes of the exemption the property must be an integral part of the watercraft, affixed or attached thereto in a substantial manner when in use."

Under this definition, numerous items which are arguably essential to a vessel's operation do not qualify as component parts. Obvious examples are charts and maps, tide tables, tool kits (hammers, wrenches, screwdrivers and the like), as well as portable fire-fighting, galley and navigation equipment.

Regulations adopted by the Board have the force and effect of law. (See Agricultural Labor Relations Board v. Superior Court, 16 Cal.3d 392.) Dictionary definitions do not. Since the forklifts do not meet the regulation's definition of "component part," they do not qualify for exemption, even if they might be considered components under some other definitions.

2. [redacted] also alleges that the federal government has classified the forklifts as "capitalizable" parts of the vessel's construction, and as "permanent" or "integral parts" of the vessel. We note in passing that the Maritime Administration's letter regarding the maintenance subsidy is the only available evidence of federal action. For purposes of this letter, however, we assume that [redacted] allegations are correct.

The point of [redacted] argument is not immediately obvious. Apparently, [redacted] believes that the federal rulings should take precedence over Regulation 1595. If that is the argument, we disagree.

The government classifications were made under federal laws authorizing construction and maintenance subsidies. The federal laws are designed to promote the national maritime industry and certainly have nothing to do with California's Sales and Use Tax Law. We also note that the standards for interpreting such laws are different from those we are required to apply: Tax exemptions are to be strictly construed against the taxpayer (Good Humor Co. v. State Bd. of Equal., 152 Cal.App.2d 879), and we know of no comparable rule for construing maritime subsidy authorizations. Accordingly, the federal classifications do not overrule Regulation 1595's definition of "component part."

3. Finally, _____ points out that lifeboats are regarded as component parts of watercraft under Regulation 1595. _____ argues that forklifts are no less "affixed or attached" than lifeboats.

Again, we disagree. Lifeboats are used on a standby basis whenever a ship is at sea, to provide a measure of protection in the event of an emergency. While they hopefully are not affixed to the vessel when functionally used, they are affixed in substantial manner when used for standby purposes. The forklifts, on the other hand, are merely stored and not otherwise used for any purpose while the ship is at sea. They are useful only when the ship is in port, and they are not affixed or attached to the vessel in any manner at that time. Accordingly, the analogy between forklifts and lifeboats must fail.

We also note that forklift trucks are listed in the Board's pamphlet number 40, Tax Tips for the Watercraft Industry, page 13, as taxable items which do not qualify for exemption as component parts of watercraft.

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As requested, you may furnish a copy of this memo to the taxpayer. However, _____ should not release anything to _____ unless the taxpayer has expressly waived confidentiality.

JEM
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