

M e m o r a n d u m**190.1428**

To: Oakland Auditing (LFF)

Date: August 11, 1978

From: Headquarters – Legal (MHH)

Subject: G--- C--- Inc. of Northern California
SS --- XX XXXXXX
Construction Contractors

Your memorandum of May 31, 1978 states that the referenced taxpayer is engaged in designing, engineering, manufacturing and installing conveyor systems in warehouses and other places. The guidelines contained in Annotation 190.1430 require clarification in the three instances cited as to classification of the system and components, and as to guidelines for determining taxable fabrication labor charges.

Annotation 190.1430, authored by Tax Counsel John H. Murray on 3-21-77, holds as follows:

- a) Conveyor systems are fixtures;
- b) Structural supports for the system are materials (supports, legs, beams, etc.);
- c) Catwalks and platforms attached to the supports are materials.

This annotation is consistent with Regulation 1521 which lists “conveying units” as fixtures in Appendix B.

In the recent case of Jervis B. Webb Company of California vs. State Board of Equalization (Los Angeles Superior Court No. C 75232, July 1978) the court sustained the Board’s classification of conveyor systems as fixtures and therefore improvements to real property rather than as machinery and equipment as claimed by the taxpayer.

That case involved conveyors for mail handling and material handling which have some similarities to the two systems you inquire about. The individual conveyors were as long as 200 feet, made up of ten-foot modules. The sections were four inches thick, ten feet long, 28 inches

wide, and mounted on supports to provide a working elevation or conveying elevation of 30 inches. In some installations the conveyors were mounted on ceiling supports, and others, on floor supports. Some of the conveyors were 100 feet long; others were 200 feet long. One thousand modules weighing 200 lbs. each were used in one installation. The modules were transported to the jobsite in ten-foot lengths, where they were assembled to make up a 200-foot system as the modules were installed. In some installations, the modules were shipped with rollers mounted in them; in other installations they were shipped without rollers because the weight would be too heavy for efficient handling in the field.

Fabrication labor is discussed in Regulation 1521(b)(2)(B)2.b. It states that jobsite fabrication labor and its prorated share of manufacturing overhead must be included in the sale price of fixtures. It further states: “Jobsite fabrication labor includes assembly labor performed prior to attachment of a component or a fixture to a structure or other real property.”

Based on Regulation 1521 and prior holdings of the Board, the guidelines for determining taxability of labor charges on fixtures would be:

Taxable fabrication includes:

1. Labor in the shop;
2. Labor at the jobsite which is performed before the item worked on is attached permanently to
 - a) A structure;
 - b) Realty;
 - c) That which is attached to a structure or realty.

This “labor” would include fabricating, assembling, processing, or other activity short of the act of attaching it to the structure, realty, or attachment to a structure or realty.

NOTE: Labor charges for jobsite reassembly of a fixture which originally was completely assembled at the manufacturing plant but disassembled for shipment is NOT fabrication labor. See Annotation 435.0140 dated 11-14-67.

Nontaxable installation includes:

1. Permanently attaching a component of a fixture or a fixture unit to
 - a) An installed component;
 - b) An installed fixture unit;

- c) A structure;
 - d) Realty;
 - e) That which is attached to a structure or realty.
2. Other labor directly essential to performing the attachment described in 1.

We will discuss your specific questions in light of the foregoing and Regulation 1521(c)(5) relating to elevators, escalators, and moving sidewalks, which are somewhat analogous to conveyors.

1. Conveying System of United Parcel Service, Exhibit A:

The structure that houses the conveying system covers an area approximately four to five acres square. The large building contains a maze of conveyors. You mention conveyor components such as rollers, bearings, idlers, etc., and inquire to what extent would the “conveyor” be classified as a fixture. You note that the belting is supplied by the building owner with installation by the taxpayer.

- (a) The entire conveyor system constitutes a permanent improvement to real property which is composed in part of “materials” and in part “fixtures”.
- (b) The portions of the system which are attached to realty and form the foundation and supporting structure for the system constitute materials. These include the 4 X 4 steel posts with their attachments to the floor, the gratings and catwalks, and any other construction materials which are attached to the framework and serve a function identified with the physical or structural support of the conveyor, rather than with the moving parts of the conveyor system.
- (c) Items such as rollers, bearings, idlers, motors, and other operating mechanisms, and other components which constitute part of the moving and transporting machinery, are fixtures.
- (d) Charges for attaching the owner-furnished belting would be taxable if they meet the guidelines of “taxable fabrication” set forth above. It would appear, however, that they do not.

2. Overhead Conveyor System at the Port of ---, Exhibit B:

We understand that on June 21, 1978 Mr. C--- O--- was advised by Mr. Gary Jugum that this conveyor system was a fixture. The questioned portions of this system are the pulleys, bearings,

motors, and a steel framed affair which appears to house the conveyor as well as supporting a catwalk and railing.

The same general rules apply to this installation. The tall structure that appears to be a building would be composed of materials generally, as would the concrete and steel framework which provide an above-ground support for the conveyor itself. Pulleys, bearings, motors, and similar items render a function to the conveyor mechanism itself, and are therefor components of fixtures and would be classified as fixtures. Catwalks and railings constitute a part of the structure attached to real property and would be materials.

The same general rules apply to fabrication labor. Labor involved in attaching components of an unattached fixture to each other, and to the unattached fixture, constitute fabrication labor. Labor involved in attaching the completed components to attached components or the supporting concrete and steel structure would be installation labor.

2. Jet Engine Repair Stand, Photograph Exhibit C:

This is an installation approximately 20' x 20' x 20'. The basic structure consists of four steel "I" beam corner posts permanently attached to the floor of a building, connected at the top by other steel framework, from which other steel units depend. The depending units are attached to the upper framework by a crisscrossing mechanism which permits the units to be moved in several directions. Attached to these units is a trolley mechanism supplied by the owner. It is this mechanism to which the engines under repair are attached.

We would classify this engine repair stand as a permanent improvement to real property. The four corner posts and the overhead connecting beams to the posts would constitute the structure and be classified as materials. Those attachments to this structure which are movable, as well as the attached mechanism for raising, lowering and moving these units, would be classified as fixtures, as would any motors or electrical fixtures which activate the movement.

The moving portion of this structure is somewhat analogous to overhead cranes. We are mindful that the appendix to Regulation 1521 lists moving parts of cranes as machinery and equipment under Appendix C. However, Annotation 565.0360 (9-4-64) classified moving parts of cranes as "fixtures" under Ruling 11, and as either fixtures or machinery and equipment under Ruling 12, depending upon the use of the cranes.

In a February 17, 1976 letter to Orange County Auditing regarding G--- C---, Inc., Tax Counsel T. L. Hartigan referred to the 1964 annotation and pointed out the apparent inconsistency with Annotation 565.0840 dated July 10, 1953 which held that moving parts of cranes were machinery and equipment without any qualification. Both annotations, however, arose under former Regulation 1615 relating to U.S. contractors. Mr. Hartigan noted that the late expression of staff opinion should be followed, and in his letter to G--- C--- which related to M--- S---, made the following classifications under Regulation 1521:

- (1) Track fastened directly to the building - - materials;
- (2) Track suspended from the building by flexible hanger rods - - fixtures;
- (3) Carrier and hoisting machiner which travels on the track - - fixtures.

As to items 2 and 3, however, he classified them as machinery and equipment under Regulation 1615, but his classification predated the April 1, 1976 amendment to Regulation 1521. As of the present time, these items (1, 2 and 3) would bear the classification shown above, whether installed by U.S. contractors or non-U.S contractors. Our classification of the engine repair stand and components is consistent with Mr. Hartigan's opinion based on Regulation 1521.

I trust the foregoing is of assistance. If further clarification is required, please contact us again.

MHH:ss

cc: Orange County – Auditing (Joan Albu, Eval. & P.)
Les Sorensen
John Murray
Don Hennessy
Jim Mahler