

Principals in the successor and predecessor are related.

The petition and protest is over the reaudited¹ measure of tax on the sales and installations of various types of signs, and not the fact of successor liability.

Contentions

In the petition and late protest dated July 19, 1983, Ms. F--- stated that after the original audit was made the records of R--- P--- were organized and show the sales and matching costs to sales for the audit period, and they show a much lower tax liability. She requested that the audit be returned to the field for presentation of additional documentation to be made available. This was done and it resulted in the reaudit.

In addition to the foregoing, Ms. F--- contended that the audit made no distinction between the signs which are considered fixtures and those which are considered structures (freestanding pylon type signs). But, the records reflect which signs are of each type.

She also noted that during the audit period the taxpayer also sold signs which were not installed for resale to other sign companies, and these sales were not credited in the audit.

Also, since the original audit was performed, additional invoices from vendors which show tax paid at the source have been organized and are available for inspection.

At the hearing on November 30, 1984, in Santa Ana, Ms. F--- contended that not enough exempt installation was allowed in the reaudit of the R--- P--- business and that many signs that were or are structures were audited as having some fixtures attached. Also, it was believed that the exempt installation on channel letter electric signs was too low.

Summary

R--- P--- was a proprietorship business that was reorganized into a corporation; the application for the corporate seller's permit shows Mr. I--- M. R--- as the president, and the starting date to be October 1, 1981.

The auditor encountered four types of signs being manufactured during the audit period which he placed into two general categories; (1) Free Standing Signs; and (2) Wall and Building Signs. He found two types of signs in the "free standing" category which he classified as (1) "single or double-face monument signs" and (2) "pole signs".

¹ The original audit is dated August 24, 1982, and the measure of tax was \$1,451,674. There is a reaudit dated June 11, 1984, which supersedes the August 24, 1982, audit; and the reaudited measure of tax is \$253,556, and it is not reflected in the notice of successor liability. The successor is petitioning for further adjustments to the reaudit.

Monument signs were audited as consisting of only materials except the facing which was considered to be a prefabricated fixture that was installed on the monument structure. The facing is the sign itself, it contains the message to be conveyed and in order to change the message the facing has to be removed and replaced with another facing containing the changed message.

Pole signs were treated in the audit as consisting of only materials except for the sign itself at the top of the pole which was audited as a prefabricated fixture. Generally speaking, the sign at the top of the pole was considered by the auditor to be analogous to the facing that is affixed to the structure portion of a monument sign.

In a report on a discussion of the reaudit it was noted that:

Taxpayer disagrees with reaudit adjustments for understated taxable sales based on law interpretation for fixtures vs. materials. Taxpayer considers all free-standing signs (pole signs and monument signs) as materials since she believes all items become a component part of real property and they lose their identity in becoming materials. Taxpayer is basing contention on derivatives from sales and use tax annotations as published by Commerce Clearing House.

Auditor is of the opinion that certain parts of signs are materials and other parts are fixtures...based on Regulation 1521 and annotations. Thus, auditor considered method of attachment and removal of certain items in constructing free-standing signs and also where fabrication of parts of signs took place, i.e. shop or jobsite. Under these guidelines the auditor was able to establish a percent of free-standing signs to be materials and the rest as fixtures. Taxpayer agrees with audit procedures and figures obtained, but still disagrees with the idea of any items being considered fixtures in regards to free-standing signs.

In the reaudit the auditor had the taxpayer break down costs involved with materials and fixtures involved. Then, by taking a percentage of materials involved in free-standing signs compared to fixtures (with related fabrication labor) resulted in 62.86 percent of materials involved. This percent was then used to separate recorded sales on Schedule R12B for a material cost accountability test.

The auditor allowed all materials which actually became a component part of the sign and is attached in such a way that they would not be readily removable. The only fixture portion involved is the facing of free-standing (monument) signs because the concrete base and other angle iron materials involved were permanently affixed to the realty. The frame of the sign is brought to the jobsite and welded together with the base of the frame welded to angle iron on top of the concrete base, and auditor considered that the only portion of the monument sign which is removable was the facing of the monument.

On schedule R12B, page 2, the auditor explains how he audited the two categories of wall and building signs (prefabricated illuminated and non-illuminated signs attached to buildings and channel-letter signs affixed to buildings.)

In respect to the reaudit the auditor noted that subsequent to the original audit additional records were located and taxpayer's representative prepared a sales journal based on all available records for 1979 and 1980. The auditor traced entries to original documents to verify accuracy of recording and segregation of types of transactions (wall and building signs, free-standing signs, resales, out-of-state sales, repair labor and detail sales).

XYZ letters were mailed to those resale customers for whom timely resale certificates or appropriate purchase orders could not be found. All questioned resales were supported and primarily involved sales to other sign companies. This explanation appears at R-12A-1, page 2.

The auditor broke down the Wall and Building Sign category into two groups; (1) illuminated or non-illuminated signs attached to buildings, and (2) channel-letter signs consisting of individual letters (generally illuminated individually) which are permanently affixed to the wall of a building. Both of these were considered prefabricated signs and audited as such.

The wall and building signs were audited as fixtures with ten (10) percent of the selling price allowed as exempt installation labor for the prefabricated illuminated and non-illuminated signs. The channel-letter signs were audited as prefabricated fixtures with twenty (20) percent of the contract price allowed as installation labor.

There does not appear to be any dispute over the way the wall or building prefabricated illuminated and non-illuminated signs were audited. However, there does appear to be some question on how the channel-letter signs were audited. In short, the problem is in the amount of prefabrication labor and installation labor that was set up.

Conclusions

We conclude that the auditor has correctly audited the pole signs. The pole signs are not entirely "structures". The pole portion is a structure and was audited that way. The prefabricated sign on top of the pole which is affixed (installed) after the pole is constructed is to be treated for audit purposes as a fixture (a prefabricated fixture) that is attached in such a way that it is not readily removable, but which can be removed and replaced with another prefabricated sign containing a different message without any dismantling or damage to the pole itself.

As noted, monument signs were looked upon by the auditor as being analogous to the pole signs. In other words, the monument itself was analogous to the pole and the facing that was affixed to the monument was deemed to be a prefabricated fixture analogous to the prefabricated sign that is placed on top of the pole. We do not agree with this.

The facing on a monument sign is attached or affixed in such a way that it is not readily removable. However, petitioner has submitted a blueprint drawing of the monument sign that was audited in petitioner's case. The blueprint submitted contains step-by-step illustrations of the construction of the monument sign which, in this case, has been identified as [letters]. [Letters] are three letters that appear on the face of the sign. The nine illustrated steps in construction are briefly described under each illustration as follows:

1. Dig sign-footing hole and install electrical conduit to customer service.
2. Call for concrete and install pipe in footing (pour concrete base of the monument).
3.
 - a. Assemble and weld together sign frame pieces and weld to pipe.
 - b. Install transformers, etc.
4. Install and bolt background to frame structure (background is the sign facing without any letters, etc.). Locate and drill holes for letters and panels (both sides of sign where it is a "double face" monument sign).
5. Install metal letters and panels to background (both sides of sign).
6. Install neon (tubing) and wire to transformers (both sides of sign).
7. Install and secure ple (plexiglass) faces (letters) to service holes (holes drilled in step #4)....same with the panel portion of the sign.
8. Assemble and install base (base of monument to lower area of sign frame).
9. Final hook up and touch up of entire sign and base cover.

The foregoing monument sign appears to be a structure in and of itself except for the panel that was prefabricated and installed. It is a panel containing the words "A Health Maintenance Organization."

Above the panel sign appear the letters "X" "Y" "Z" which, alone or individually do not constitute a fully prefabricated sign. They are very much like channel letters affixed to the face (background) of the monument. The entire sign, with the exception of the panel sign portion appears to be constructed in place and until it is complete (after step #9) it is not a sign; instead, it is a structure under construction. We, therefore, conclude that the only portion of the monument sign that is a fixture in this example is the prefabricated panel sign containing the words "A Health Maintenance Organization." The panel could be removed and replaced with another panel containing a different message without dismantling or damaging the rest of the monument structure. The letters are an integral part of the background or face and they would have to be removed piece by piece and if a different message (different letters) were to be installed new holes would have to be drilled to accommodate what letters might be installed to replace the letters "X, Y, Z".

In summary, as far as this example is concerned, only a very small part of the whole should be audited as a fixture and that would be the prefabricated panel portion on the facing or background, the rest should be audited as materials and there would be very little installation labor of the panel portion of the sign.

Channel-letter signs have been considered in other audits and petitions of sign manufacturing companies. Their signs and installations are basically the same. Generally, they are not totally prefabricated letters (like the [letter] sign) that requires nothing more than a simple installation or attachment to the wall. The completed illuminated sign itself is made up of several components such as plexiglass, plastic channel letters, neon tubes, transformer, housing, conduit, and wiring, which are installed in a series of steps. Note: the transformer component is a fixture, all else is materials.

It has been shown that there are approximately eleven (11) steps involved in the installation of each letter of a channel-letter sign. There is no prefabricated sign (fixture) delivered to the jobsite in channel-letter sign installations. A test in another similar matter showed that if material costs were considered the taxable measure (i.e. plywood, metal, plastic, channel letters, neon tubes, transformer, housing, conduit and wiring), only twenty-six (26) percent of the selling price of the sign would be taxable. It was estimated that forty (40) percent of petitioner's sign business was channel-letter signs.

In a channel letter sign the completed sign is the fixture, not the backing, transformers, plastic letters, etc., before installation. In other words a sign fixture is fabricated "in place" and as it is fabricated it is simultaneously installed so the end result is an improvement to the building (realty) to which it is attached.

Petitioner's contention with respect to the pole signs is misplaced and is apparently based on an article that appeared in the June 1980 "Tax Information" bulletin publication which is a bulletin containing sales and use tax information mailed to holders of seller's permits along with their quarterly tax return forms. The article was headed "Construction Contractors - Outdoor Electrical Displays", and it discussed (1) when signs are considered fixtures, and (2) when signs are considered structures. It provided that prefabricated wall and roof mounted signs are fixtures, and signs other than prefabricated fixtures, such as free-standing pylon type signs embedded in the ground or in some other manner attached to real property, are regarded as structures.

The choice of words in discussing "when signs are considered structures" in the Tax Information bulletin was poor because it implies that a pole embedded in the ground with a prefabricated sign attached (a pole sign) is a structure. That was not the intent of what was said.

Signs that are structures are the large outdoor advertising type signs seen along highways which are periodically changed generally by papering a new advertisement on the face of the signboard; sometimes it is called billboard advertising. There is a tax counsel opinion in the Business Taxes Law Guide dated November 7, 1964, which reads in part as follows:

190.0560 Outdoor Advertising Signs. A large outdoor advertising sign erected upon land is a structure, and the contractor is the consumer of the materials used in the sign. Signs attached to buildings are considered fixtures, becoming real property upon being affixed.

There is an unpublished tax counsel memorandum dealing with some aspects of the commercial sign business which points out where there is a sign transaction that does not involve the lease of an installed sign, the "general rules remain as follows:

In a construction contract to furnish and install an advertising sign pole, the pole is treated as materials, the prefabricated sign is a fixture. If the sign is not prefabricated, it is materials."

The foregoing general rule is to be applied to petitioner's pole, channel-letters and monument signs. Channel letter signs are definitely not prefabricated. Each letter is fabricated as it is being installed and the installation takes ten to eleven major steps before it is complete.

Obviously, letter signs attached to a building that are prefabricated (i.e. the letter is complete in itself like a bronze casting, and all that needs to be done is to affix it to the building), would be a fixture. Each individual letter is a fixture and the fact that no word may be spelled by it does not make it materials since it is in a fully prefabricated form prior to installation.

In the monument sign example the entire monument, including facing or background and letters, are materials and the only prefabricated fixture portion of the sign would be the prefabricated panel sign that was affixed.

The rule in Regulation 1521 (subsection (c)(2) relating to prefabricated cabinets is cited under "particular applications"; it only applies to prefabricated cabinets and does not apply to prefabricated signs.

The channel-letter signs are not prefabricated and then installed. The completed sign is a fixture only after is completed and that occurs only after it is completely installed. Installation labor on the channel-letter signs is substantial and should be considered exempt installation of channel-letter components with the end result being an improvement to realty. Note: the transformer component is a fixture.

Pole signs, on the other hand, involve a substantial amount of construction work prior to the installation of the prefabricated sign and it is obvious that the exempt labor portion of the job would be greater than the labor involved in installing a prefabricated wall or rooftop sign. It would appear that the pole sign job can be divided into two phases; (1) the construction of the pole on which the prefabricated sign is to be attached-phase (this is analogous to constructing a building on which a wall or roof sign is attached); and (2) the installation of the prefabricated sign to the pole-phase (this is analogous to attaching a wall sign to a building).

A monument sign such as in the example set forth herein is a structure except for any prefabricated sign (like the panel sign) that was attached to complete the message on the face (background) of the sign. The face or background for the letters and panel is a part of the whole sign and could be considered the sign itself, but the description of the construction shows that it was not prefabricated and installed as a completed sign.

Recommendation

A--- S--- & N--- S--- is the successor to R--- P---. Redetermine. Reaudit the channel-letter signs and the monument signs in accordance with the foregoing conclusions.

Reaudit and adjustments to be made by Orange County Auditing.

Robert H. Anderson, Hearing Officer

Feb 26 1985

Date