

**STATE BOARD OF EQUALIZATION**

1020 N STREET, SACRAMENTO, CALIFORNIA  
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(916) 323-7977

May 23, 1990

R--- F--- R---, Inc.  
P.O. Box XXXX  
---, California XXXXX

Dear Madam or Sir:

RE: SZ -- XX-XXXXXX-010

Enclosed is a copy of the Decision and Recommendation pertaining to the petition for redetermination in the above-referenced matter.

I have recommended that the Board staff perform a reaudit in accordance with the views expressed in the Decision and Recommendation. No action is required of you at this time, except that you are requested to cooperate with the audit staff during the course of the reaudit.

The audit staff will provide you with a copy of the reaudit report. A copy of that report will also be sent to me. At that time, I will write to you informing you of your options for appeal in the event that you disagree with the reaudit results.

Very truly yours,

W. E. Burkett  
Hearing Officer

WEB:af

Enc.

cc: Mr. L--- E. C---  
Attorney at Law  
c/o R--- F--- R---, Inc.  
P.O. Box XXXX  
---, California XXXXX  
With Copy of Hearing Decision and Recommendation  
Ms. Janice Masterton  
Assistant to the Executive Director  
With Copy of Hearing Decision and Recommendation  
Mr. Glenn Bystrom  
Principal Tax Auditor (file attached)  
--- -- District Administrator  
With Copy of Hearing Decision and Recommendation

BOARD OF EQUALIZATION

APPEALS UNIT

In the Matter of the Petition	)	HEARING
for Redetermination Under the	)	DECISION AND RECOMMENDATION
Sales and Use Tax Law of:	)	
	)	
R--- F--- R---, INC.	)	No. SZ -- XX-XXXXXX-010
	)	
	)	
<u>Petitioner</u>	)	

The above-referenced matter came on regularly for hearing before Hearing Officer W. E. Burkett on February 5, 19XX, in ---, California.

Appearing for Petitioner:

Mr. R--- C. L---  
Treasurer

Ms. M--- P---  
Controller

Mr. L--- E. C---  
Attorney at Law

Appearing for the  
Department of Business Taxes:

Mr. Spencer B. Stallings  
Supervising Tax Auditor

Ms. Eileen M Baier  
Senior Tax Auditor

Protested Items

The protested tax liability for the period January 1, 1985 through March 31, 1988 is measured by:

<u>Item</u>	<u>State, Local and County</u>
D. Disallowed exempt sales at Branch 95 – Detailed Examination	\$ 20,000
E. Taxable sales understated at Branch 95 – Statistical Sample	\$103,969

Contentions of Petitioner

- D. Charges for installation and removal are exempt from the tax.
- E. Charges for installation and removal are exempt from the tax.

Summary

The petitioner is a corporation engaged in the business of renting sprinklers, pipe, pumps and related accessories. A prior audit of petitioner was conducted through December 31, 1984.

The petitioner's protest involves the application of the tax for installation and removal charges included in the measure of tax for rental sales.

Protested item D involves a single billing to S---, Inc. of --- --- for "installation labor addition to rental #629738 to complete job in ---, CA" \$26,111.42. A copy of the parties' contract is not available.

Petitioner contends that the charges were for field layout and connection and that services occurred after the rental period began. The position of the Department of Business Taxes is that the installation occurred prior to sale and that the charge may involve field assembly labor properly classified as a sale under Revenue and Taxation Code Section 6006(b).

The second protested item consists of a number of disallowed charges for installation and removal charges made in connection with the rental of sprinklers. The protested measure of tax also includes some charges for delivery which are conceded to be subject to the tax.

The audited deficiency was computed on the basis that all "taxable" installation occurred prior to the sale and that all charges for removal were required as part of the rental service contract.

The petitioner contends that many contracts for rentals of sprinklers require that the rental period begin prior to the actual date of delivery of the property. It was explained that in the industry it is necessary to rent sprinklers for block periods to insure that they will be available for use when required. Petitioner's representatives submitted schedules for a portion of the year 1989 confirming this practice. They also presented a sample copy of the lease agreement. This agreement does not specifically deal with installation although it specifically requires the "rentee" to pay for delivery and return of the leased property.

Petitioner's Controller, M--- P---, advised that installation is strictly an optional service that is contracted for in only a small portion of the lease contracts.

### Analysis & Conclusions

We first consider the various charges involved in the test used to compute the measure of tax deficiency for audit item E. The Department has applied the tax to the charge for the installation portion of the sprinkler rental contracts on the basis that the charges were mandatory service charges for services performed prior to the beginning of the lease agreement as set forth for erection of scaffolding (see Annotated Letter Ruling No. 330.3310; Business Taxes Law Guide 3223). The charge for such service is properly includable as part of the leasing sales price where performed prior to the beginning of the lease for the purpose of placing the personal property (scaffold components) in a form for leasing. In this setting, erection is considered to be a cost or expense of the lessor even though he may obtain reimbursement for the cost from the lessee. (See Revenue & Taxation code Section 6011(a)(2).) However, the charges at issue here are not for reassembly of components of personal property. Rather they are for the field layout and attachment of sprinkler pipe to the real property. The charges for such installation contracted by the customer are specifically exempt from the tax whether performed before or after the lease term begins and without reference to whether the installation service is mandatory or optional (Revenue and Taxation Code Section 6011(c)(3)). Further, a charge for the temporary field assembly of the sprinkler components would not constitute a sale of tangible personal property. There is no fabrication of components and the actual labor of assembling the sprinkler components does not constitute a step or process in the production of a property.

We reach the same conclusion with respect to the audit item D installation service and for the same reasons.

The delivery portion of the amounts denied exemption is properly subject to tax because the amounts are not separately stated as required by law and Regulation 1628, and for the additional reason that the evidence does not warrant a finding that the delivery was performed after the leasing sale began.

It is also our conclusion that no portion of the charge for removal of the leased property is excludable from the measure of tax. The return of the property to the petitioner is an express condition of the hiring contract. The performance of this service by the petitioner for an additional amount is merely an added leasing charge.

Recommendation

It is recommended that a reaudit be conducted for the purpose of eliminating all installation charges from the test and from the measure of tax deficiency.

\_\_\_\_\_  
W. E. BURKETT, HEARING OFFICER

\_\_\_\_\_  
4-26-90  
DATE