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**STATE BOARD OF EQUALIZATION**

May 27, 1964

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This is to inform you of our recommendation to the Board on your petition for redetermination of sales and use tax. It will be our recommendation that the tax be redetermined by deleting sales of tooling in cases where no title provision appears on the purchase order or invoice.

The item protested at the hearing concerned molds and dies used in the manufacture of oil seals. We believe that while a purchase order and an invoice ordinarily evidence a sale, other evidence in this case showed that this was a means of billing for tooling and, as such, was only a pricing arrangement. At the hearing, you showed that the tooling was used in producing the property which you sold, that you were responsible for any loss or destruction of the tooling, and that the tooling is not turned over to the customer at the end of the production run. We think these facts are evidence that the benefits of owning the property remain in the manufacturer and, accordingly, no sale takes place.

Where there is a specific title provision incorporated into the purchase order, we believe a sale has occurred. A purchase order is an offer which, when accepted, forms a part of the contract of sale. Any title provisions becomes an express term of the contract and binding upon the parties thereto.

This matter will be referred back to our Out-of-State office so that they may make appropriate changes in the audit. If, after the changes are made, you still wish to protest the matter, you can let us know, and we will set the matter to be heard before the Board. Our auditors will let you know of the redetermined amounts. We would appreciate hearing from you with respect to a Board hearing within 30 days of such notification. Board hearings are held monthly in Sacramento.

Very truly yours,

John H. Knowles  
Associate Tax Counsel

JHK:cr [lb]

**Memorandum****440.0340**

To: Mr. Robert L. Imig  
Torrance Audit

November 21, 1989

From: David H. Levine  
Tax Counsel

Subject: P. E. W--- & S---, Inc.  
Account No. SR -- XX-XXXXXX

This is in response to your memorandum dated October 11, 1989. Taxpayer is a machine shop that uses special tooling to manufacture requested parts. The auditor concluded that the taxpayer sold the special tooling to the customer since the customer requested the tooling, the sales invoice separately listed the tooling, and the customers believed that they owned the tooling. Also, taxpayer displayed no obvious indication of ownership such as capitalization or payment of property taxes. Taxpayer objects to this conclusion stating that it did not sell the tooling and maintaining that the separate charge was only a pricing method.

Initially, we note that we do not understand the reason for this inquiry. It helps us to understand your inquires when you explain the reason for your dispute with the taxpayer. It appears here that taxpayer may be arguing that its separately stated charge for the tooling should not be included in the measure of tax. If so, we disagree since the total sale price of tangible personal property is subject to sales tax with no deduction for the cost of materials, labor, or any other expense. (Rev. & Tax. Code § 6012(c)(2).)

As you know, the question in this area that normally arises is whether title to the tooling passes to the customer prior to the manufacturer's use of that tooling. If so, the manufacturer may purchase the tooling ex tax for resale. Otherwise, the manufacturer purchases the tooling at retail for use in manufacturing the items it sells. In the case before us, it appears that taxpayer is not arguing that it purchases the tooling for resale, and we assume that taxpayer concedes that sales or use tax is applicable to its purchase of the tooling.

In response to your specific question, the actual terms of the contract between taxpayer and its customers control whether taxpayer sells the tooling to the customers. The fact that the customers believed that they owned the tooling is not determinative if that understanding is not

consistent with the contract. Of course, the customer's understanding is relevant to the question of what the contractual terms mean. Further, if taxpayer routinely transfers possession of the tooling to its customers upon the customer's request, that is strong support that taxpayer sells the tooling to its customers. However, without reviewing the actual contractual terms, we cannot provide you with a definitive response.

Taxpayer's representative apparently believes that Annotation 440.0340 (5/27/64) supports the conclusion that the tooling was not sold to taxpayer's customers and, I assume, that the charge for the tooling is not subject to tax. That annotation concludes that a particular transaction did not involve a sale of the tooling. It continues: "In this case the invoice is only a pricing arrangement and not evidence of a sale. If the title provision appears on the purchase order or invoice, the transaction does not qualify for the sales tax exemption." Back-up material to this annotation does not shed much light. However, the annotation mentions an exemption and only makes sense in the context of an exemption for the sale of items besides the tooling. The taxpayer in that annotation was probably making a sale of manufactured goods in interstate commerce which was exempt from sales tax. The special tooling used to manufacture those items would, however, have been used in this state and the sale of the tooling or its use would have been subject to sales or use tax. If title had passed to the customer prior to the taxpayer's use, the taxpayer could have purchased the tooling for resale, but the taxpayer would have made a retail sale of the tooling to the customer for use in this state, and that sale would not have been exempt from sales tax as a sale in interstate commerce. If title to the tooling passed to the customer after the taxpayer's use, tax would apply to the sale of the tooling to the taxpayer (or to the taxpayer's use), but the sale of the tooling by the taxpayer might be entitled to the exemption for sales in interstate commerce. The conclusion in the annotation was that the taxpayer did not sell the tooling. This meant that the only sale was an exempt sale of the manufactured goods. The annotations does not stand for the proposition that a charge for special tooling which is not sold to the customer may be deducted form the measure of sales tax with respect to a taxable retail sale in this state.

As mentioned above, it appears that taxpayer's entire charge would be subject to sales tax with no deduction on account of its charge for special tooling. If, however, the underlying sale is entitled to an exemption, your question with respect to title passage does become relevant. If so, and if you wish us to consider this question further, please forward copies of the relevant contractual documents. But we also note that it is certain that tax would apply to at least one sale of the tooling (either the sale to the taxpayer or the sale by the taxpayer to its customer).

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