



STATE BOARD OF EQUALIZATION

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August 15, 1994

BURTON W. OLIVER
Executive Director

Mr. W--- R. L---
L--- C--- Company
XXX --- Avenue
---, CA XXXXX

Re: **SR --- XX-XXXXXX**

Dear Mr. L---:

I am responding to your letters of May 7, 1994 and July 15, 1994 regarding the application of sales tax to your business. I apologize for the delay in answering your letter.

You make cabinets, and you sell most of them to general contractors. You furnish and install of the remainder of the cabinets and also perform repairs, interior trim and similar tasks. You ask whether you may issue a resale certificate to your suppliers and purchase all your materials for resale, regardless whether you consume or resell the materials. You also ask how tax applies when you furnish and install cabinets.

A. Purchase for Resale

Revenue and Taxation Code section 6051 imposes a sales tax on all retailers measured by their gross receipts from retail sales of tangible personal property occurring in this state, unless the sale is otherwise excluded or exempted by statute. When sales tax does not apply, use tax applies to the use of property purchased from a retailer for use in California. (Rev. & Tax. Code §§ 6201, 6401.) A retail sale is a sale for any purpose other than resale in the regular course of business. (Rev. & Tax. Code § 6007.)

A person such as yourself who is registered by the Board as a seller may purchase property extax for resale by issuing a resale certificate provided the property is purchased for resale in the ordinary course of business. If a person makes any use of the property purchased under a resale certificate, that person owes use tax. (Rev. & Tax. Code § 6094(a).)

Your first question is whether you may issue a resale certificate to the suppliers and purchase all materials for resale, whether for consumption or resale. You may issue a resale certificate only when purchasing the materials as a fungible, commingled lot, a significant portion of which you intend to resell and a portion of which you will consume, but at the time of your purchase you do not know which items you will consume and which you will resell (i.e., they are all placed in a resale inventory and removed for sale or use as needed). However, if at the time of your purchase you know that certain materials will be consumed in the performance of a construction contract, you may not issue a resale certificate with respect to those materials. The sale to you of such materials will be subject to sales or use tax.

B. Installation of Cabinets

As discussed below, your contracts to furnish and install cabinets are construction contracts. Sales and Use Tax Regulation 1521 explains the application of California sales and use tax to construction contracts. A construction contract includes a contract to furnish and install property becoming an improvement to real property. (Reg. 1521(a)(1)(A)1.) Subdivision (a)(1)(B)2 excludes from the definition of construction contract those instances where the contracting party furnishes the property but is not responsible for the final affixation or installation of the property. Since you both furnish and install cabinets onto real property, your contracts to do so are defined by the regulation as construction contracts and you are a construction contractor.

Regulation 1521 defines the terms "materials" and "fixtures" as those terms apply to construction contractors. Materials are construction materials and components, and other tangible personal property incorporated into, attached or affixed to real property, such as a building, by a construction contractor, which when combined with other tangible personal property lose their identity to become an integral and inseparable part of the real property. (Reg. 1521(a)(4); see also Reg. 1521, Appendix A.) A construction contractor is generally the consumer of materials which the contractor furnishes and installs in the performance of a construction contract. Tax applies to the sale to, or use by, the contractor of those materials. (Reg. 1521(b)(2)(A)1.)

"Fixtures" are defined by Regulation 1521 as items which are accessory to a building or other structure and do not lose their identity as accessories when installed. (Reg. 1521(a)(5); see also Reg. 1521, Appendix B.) In general, a construction contractor is the retailer of fixtures which the contractor furnishes and installs in the performance of a construction contract, and tax applies to the sale of the fixtures by the construction contractor to a customer. (Reg. 1521(b)(2)(B)1.) Tax does not apply to charges for installing fixtures. (Reg. 1521(b)(2)(B)2.)

For California sales and use tax purposes, when cabinets are furnished and installed pursuant to a construction contract, they are sometimes considered materials and sometimes

considered fixtures. Regulation 1521(c)(2) states a specific rule for determining whether a cabinet is materials or a fixture. A cabinet is considered to be a fixture when 90 percent of the total direct cost of labor and materials used for fabricating and installing the cabinet is incurred before the cabinet is affixed to the real property. In determining this 90 percent, the total direct cost of all labor and materials used in fabricating the cabinet to the point of installation is compared to the total direct cost of all labor and materials used in completely fabricating and installing the cabinet. (Reg. 1521(c)(2).) If less than 90 percent of the total direct cost for labor and materials to make and install a cabinet is incurred before the cabinet is affixed to the real property, the cabinet is considered materials.

If a cabinet is considered materials, tax applies to the sale to or use by the construction contractor of those materials used in furnishing and installing the cabinet. If the contractor purchases those materials without paying sales tax reimbursement or use tax to its vendor (e.g., if they are purchased under a resale certificate because part of a fungible, commingled lot of materials, a significant portion of which would be resold), the contractor must report use tax on line 2 of its Sales and Use Tax Return.

If the cabinet is considered a fixture, tax applies to the sale price of that cabinet to the construction contractor's customer. (Reg. 1521(b)(2)(B)2.) If the contract states the sale price for which the prefabricated cabinet is sold, tax applies to that price. (Reg. 1521(b)(2)(B)2.a.) If the contract does not state a sale price, the sale price is deemed to be the cost price and tax applies to that cost price. For a contractor like yourself, who manufactures his own fixtures, the cost price is deemed to be the price at which similar fixtures in similar quantities ready for installation are sold by the contractor to other contractors, or, if the contractor does not make this kind of sale, the amount stated in the contractor's price lists, bid sheets or other records. (Reg. 1521(b)(2)(B)2.b.) If the cost price cannot be established in this way, it is established by an aggregate of the cost of materials, direct labor, overhead costs and a reasonable profit, as detailed in subdivision (b)(2)(B)2.b.[1]-[6] of Regulation 1521. In your situation, you apparently do sell the same type of cabinets you install to other contractors, ready for installation. Thus, if you furnish and install cabinets regarded as fixtures and your contract does not state the sale price, the taxable sales price will be the amount you charge other contractors for the same cabinets.

You give one example where extensive on-site fitting of a corner cabinet is required. You will charge \$800, \$650 of which is the charge attributable to the cabinet. The calculation discussed above for determining whether a cabinet is a fixture or materials is based on the contractor's cost, not the charge to the customer. Assuming that your total direct cost of material and labor up to the time of installation is less than 90 percent of your total direct cost, including installation, tax is due on only on your cost of materials. If you had purchased those materials without having paid sales tax reimbursement or use tax to your vendor (e.g. under a resale certificate), you must report that cost on line 2 of your Sales and Use Tax Return. On the other hand, if your direct cost of installation does not exceed 10 percent of your total direct cost of

Mr. W--- R. L---

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materials and labor for furnishing and installing the cabinet, the cabinet is a fixture and you are the retailer. You owe sales tax on the sales price of the cabinet, as discussed above. Please note that the determination of whether a cabinet is a fixture or materials is done on a cabinet by cabinet basis.

If you have further questions, feel free to write again.

Sincerely,

Victor G. Matl
Tax Counsel

VGM:plh

cc: Sacramento District Administrator - KH