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Memorandum

To: Mr. Mike Hilbert
Aerospace Co-ordinator
Audit Eval. & Plan.

Date: July 9, 1969

From: John L. Waid
Tax Counsel

Subject: Aerospace Title Clauses

I am writing this in response to your memorandum to me of May 27, 1992. You attached two memoranda from Mr. Gene Schaffer, a tax auditor in the San Diego district office. Mr. Schaffer has requested an opinion on the efficacy of certain title-passage clauses which he accepted as valid under the decision in Aerospace Corp. v. S.B.E. (1990) 218 Cal.App.3d 1300 to accelerate title to property purchased by government contractors for use in performance of their contracts to the United States prior to use by the contractor. He also had a question regarding overhead charges by a corporation related to a government contractor.

OPINIONA. Related Corporation

As I understand it, Corporation A, which has no government contracts, is a related corporation to Corporation B ("Corporation B"), which does. They apparently share overhead expenses, and Corporation B passes these overhead expenses on to the United States. We are assuming that Corporation B's contracts contain the required title-passage clauses.

As you know, under Aerospace, title to overhead materials purchased by a contractor the cost of which are allocable to its government contracts passes to the government prior to use by the contractor when the appropriate title clauses appear in the taxpayer's contracts with the federal government. Indirect costs, to be valid, must be properly allocable to the particular contract. (FAR 31.201-1 & 31.201-4.) Corporation A is a separate legal entity and not a party to Corporation B's contracts; none of its overhead expenses may be allocated to Corporation B's contracts.

B. Title-Passage Clauses

1. 52.232.7007. This clause is not found in the FAR but the title-passage provisions are identical to those of the Progress Payments Clause (FAR 52.232-16(d)), the

terms of which are the same as those at issue in Aerospace. Therefore, this clause will operate to pass title to contractor-acquired property to the United States prior to the contractor's use.

2. 252.217-7106. Again, this clause is not found in the FAR, but, like the previous clause, may be derived from one in an agency supplement. It provides for the making of progress payments and, in subdivision (e), provides for title-passage as follows:

“All materials, equipment, and other property or work in process covered by progress payments made by the Government shall upon the making of such progress payments become the sole property of the Government, and shall be subject to the provision of [a title clause in the contract].”

The progress payments will be determined on the basis of “the value, computed on the price of the job order, of labor and materials incorporated in the work, materials suitable stored at the site of the work, and preparatory work already completed...” (52.217-7106(a).) It is contemplated, then, that the payments will not be made until some portion of the work has already been done and the property used in performance of the contract. Title does not pass to the United States until payment is made. Thus, the contractor is using its own property to perform the contract, and is consuming the property it purchased for that purpose. Tax thus applies to its purchases of such property.

3. FAR 52.232-13 is not a title-passage clause. It does, however, require suspension of the Progress Payments Clause, FAR 52.232-16, under certain conditions. Thus, when those conditions occur, there is no accelerated title-passage.

JLW:es

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