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**STATE BOARD OF EQUALIZATION**

May 8, 1967

Dear Mr. REDACTED TEXT,

We regret our delay in responding to your letter of December 20, 1966. Mr. John Quick, District Principal Auditor of the Los Angeles area, has since forwarded the letter to our legal staff for direct reply to you.

It is our understanding that your client, "S" (herein, taxpayer) entered into a cost-reimbursement contract with the U.S. Government on June 16, 1966. We assume that the taxpayer purchases equipment and materials to be used under the contract, ex tax for resale to the U.S. Government. Article 18, clause (c) of the contract provides, in part, that:

"Title to all property purchased by the contractor, for the cost of which the contractor is to be reimbursed as a direct item of cost under this contract, shall pass to and vest in the Government upon delivery of such property by the vendor."

Specifically, you ask whether purchases of tangible personal property under the above-described circumstances constitute exempt sales for resale to the U.S. Government within the meaning of Section 6381 of the California Sales and Use Tax Law.

As indicated in Sales and Use Tax Ruling 13, copy enclosed, the term "cost-plus-a-fee war materiel contract" means a contract with the U.S. to furnish, or to fabricate and furnish, tangible personal property for cost in accordance with which the U.S. takes title to all tangible personal property purchased for use in fulfilling the contract immediately upon or prior to delivery of the property to the contractor, the contractor being reimbursed by the U.S. for the actual cost and the U.S. having control over the property from the time title is vested in the U.S. The same principles apply to other cost reimbursement contracts with the U.S.

Applying this test to the above-quoted title clause, it would appear that title to property for which reimbursement is paid as a direct cost passes to the U.S. Government upon delivery by the vendor, and, prior to any use by the contractor before his resale of the property to the Government. Accordingly, we believe that sales of this equipment and material under a standard cost reimbursement U.S. Government contract with an appropriate title clause, constitute exempt sales for resale under Ruling 13.

We assume that the "other property" referred to in clause (c) of Article 18 in the subject contract relates to "indirect" or "overhead" materials and supplies. Our review of the contract shows that indirect or overhead costs are not part of the "allowable costs" (see Article 12(2)) to be reimbursed to the contractor by the U.S. Government. This conclusion stems from the fact that the contract states that indirect or overhead costs are not included in "allowable costs". We assume the initials "N.A." mean "not applicable". Accordingly, title to this "other property" would not pass to the

U.S. Government pursuant to the title provision found in the third sentence of clause (c) of Article 18. Of course, if there are any "overhead" or "indirect" supplies acquired for use under the contract by the contractor, their tax status would be governed by Sales Taxes General Bulletin 59-9, copy enclosed.

It should be noted that in giving our opinion, we have assumed that none of the property is purchased by the contractor for use in constructing improvements on or to real property.

Very truly yours,

E. H. Stetson  
Tax Counsel

By Elliott D. McCarty

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