C&S COMPONENTS, INC. P.O. Box 538 Clanton, AL 35046-0538,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Taxpayer,	§	DOCKET NO. S. 01-300
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

OPINION AND PRELIMINARY ORDER

The Revenue Department assessed C&S Components, Inc. for State and local sales tax for May 1997 through May 2000. C&S Components appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on August 8, 2001. Attorney Tim Davis and CPA Edward Taylor represented C&S Components. Assistant Counsel Margaret McNeill represented the Department.

ISSUE

The issue in this case is whether C&S Components owes Alabama and City of Clanton sales tax on materials that it purchased from out-of-state vendors, fabricated or otherwise prepared for use at its Clanton, Alabama facility, and then used in constructing gasoline pump canopies outside of Alabama.

FACTS

C&S Manufacturing, Inc. and C&S Components, Inc. (together "C&S") are commonly owned and have a joint facility in Clanton, Alabama. During the period in question, C&S furnished and installed gasoline pump canopies for the convenience store industry in the Southeastern United States. Before 1997, the business operated as C&S Manufacturing. C&S Components was incorporated in February 1997 to act as purchasing agent for the business. C&S Components obtained an Alabama sales tax license, and began collecting sales tax from its customers on its

materials and labor charges. It remitted the tax to the state and local taxing jurisdictions in which the canopies were installed. C&S claims that it obtained a sales tax number and began paying sales tax as indicated above at the suggestion of a Department examiner in 1996.

C&S operated as follows during the period in issue:

Independent salesmen that represented C&S called on various oil jobbers and convenience store operators in the Southeastern United States. If a customer needed a canopy for a new or existing location, C&S would prepare a joint quote for the job, which included furnishing all materials and installing the canopy at the customer's location.

Once the customer agreed to the quote, C&S Components ordered the major components needed to fill the order, generally from out-of-state vendors. Because each canopy had unique dimensions and requirements, C&S Components did not maintain an inventory of major components, but rather custom-ordered the components as needed for each job. It did maintain an inventory of caulking, screws, canopy lights, and other miscellaneous materials at its Clanton facility that were withdrawn and used on the jobs as needed. C&S Components purchased all materials tax-free during the audit period using its Alabama sales tax number.

The vendors drop shipped the components either directly to the job site, or, if the materials needed to be further prepared for use, to the C&S facility in Clanton. If the components were shipped to Clanton, they were immediately segregated by job number and prepared for use on the job. They were subsequently shipped to the job site, where C&S Manufacturing assembled and bolted the canopies in place.

C&S Manufacturing and C&S Components jointly billed each customer for the completed job, which included materials, labor, freight, and installation. As indicated, C&S charged the customer the applicable sales tax on the materials and

labor charges, and remitted the tax to the state and local jurisdictions in which the canopy was installed.

The Department audited C&S Components and assessed it for Alabama sales tax on its cost of the components that were purchased out-of-state, delivered to the Clanton facility for preparation, and then shipped to a job site outside of Alabama. It also assessed City of Clanton tax on those components, and also on the components that were first shipped to Clanton and then used on in-state jobs. According to the Department, the components were taxable under the sales tax "withdrawal" provision, Code of Ala. 1975, §40-23-1(a)(10), when C&S withdrew the components from inventory in Clanton for use on the furnish-and-install contracts.

The Department did not assess C&S on the materials drop shipped by a vendor directly to an out-of-state job site. The Department claims in its audit report that C&S had erroneously paid tax at the point of installation (job site) instead of the point of withdrawal (Clanton)[1], and also that tax was due on only the cost of materials, and not labor. The Department suggested that C&S and its customers could file joint petitions for refund concerning the tax erroneously paid on the labor charges. The audit report also suggested that because C&S Components does not make retail sales, it should close its sales tax account and apply for a use tax number, which it did.

C&S Components concedes that it owes sales tax on its cost of the caulking, screws, canopy lights, etc. that it withdrew from general inventory in Clanton and used on the contracts. It contends, however, that the major components that were shipped to Clanton, prepared for use, and then shipped outside of Alabama were

[1]Presumably, that statement pertains only to the materials delivered to and prepared for use in Clanton before being shipped to the job site. Those materials delivered directly to the job site obviously could never have been withdrawn from inventory in Clanton. I assume that in those cases, the Department agrees that tax was due at the job site, although the applicable tax would be use tax, not sales tax.

not subject to either Alabama or Clanton tax because they were only temporarily stored in Clanton, citing the Department's "temporary storage" regulation, Dept. Reg. 810-6-5.23.

ANALYSIS

The sales tax "withdrawal" provision, §40-23-1(a)(10), applies if a taxpayer purchases tangible personal property at wholesale and subsequently withdraws the materials from its general inventory for personal use or consumption. The taxable measure is the taxpayer's wholesale cost of the property. See, Dept. Reg. 810-6-1-.196. For example, if a taxpayer contracts to furnish and install building materials in the form of real estate, and also sells building materials over-the-counter at retail, the taxpayer is allowed to purchase all materials tax-free. The taxpayer would then owe sales tax (1) on its wholesale cost of the materials withdrawn from inventory and used on the furnish-and-install contracts, and (2) on the retail sales price charged to the over-the-counter customers. See generally, *City of Huntsville v. City of Madison*, 628 So.2d 584 (Ala. 1993). For a detailed history of the withdrawal provision, see *American Chalkboard Co., LLC v. State of Alabama*, S. 99-473 (Admin. Law Div. 10/3/00).

In this case, C&S does not make retail sales, and, except for various miscellaneous items, does not maintain a general inventory of materials. Consequently, the withdrawal provision does not apply. Rather, C&S is a contractor, as that term is used in §40-23-1(a)(10), which defines "retail sale" to include "[s]ales of building materials to contractors, builders, or landowners for resale or use in the form of real estate are retail sales in whatever quantities sold." C&S is a contractor under the above provision because the canopy components are building materials which are bolted to and become a part of real property. See generally, *Dept. of Revenue v. James A. Head & Co., Inc.*, 306 So.2d 5 (Ala.Civ.App. 1974); *American Chalkboard Co.,* S. 99-473 at 4, 5.

As a contractor that does not make retail sales, the Department examiner correctly advised C&S Components to close its Alabama sales tax account. C&S Components should pay sales tax when it buys the materials from its vendors. See, Dept. Reg. 810-6-1-.27. If it buys the materials outside of Alabama, obviously no Alabama sales tax would be due. But if C&S subsequently uses the materials on an Alabama job, Alabama use tax and also local use tax, if applicable, would be due. The taxable measure would be C&S's cost of the materials. C&S would be allowed to off-set the Alabama use tax by a credit if any sales or use tax was previously paid to another state on the materials. Code of Ala. 1975, §40-23-65.

Concerning the components in issue that were purchased from out-of-state vendors, prepared for use at the C&S facility in Clanton, and then delivered to out-of-state job sites, the issue is whether the temporary presence of the components in Clanton was sufficient to subject them to Alabama and Clanton use tax.

The temporary storage exclusion from use tax applies if the property was at all times intended for use outside of Alabama and was subsequently used solely outside of Alabama. Dept. Reg. 810-6-5-.23; Code of Ala. 1975, §40-23-60(7) ("storage" defined as "any keeping or retention in this state for any purpose except . . . (for) subsequent use solely outside this state . . . .").

C&S intended for the components in issue to be used outside of Alabama. It could be argued, however, that the temporary storage regulation does not apply because the components were "used" in Alabama when C&S prepared them for use in Clanton before shipping them to the out-of-state job sites.

Alabama's courts have never addressed the issue of whether a taxable "use" occurs for use tax purposes when property is brought into and prepared in Alabama for its ultimate purpose, but is later transported and used for its intended purpose outside of Alabama. I agree with the Wyoming Supreme Court's rationale in *Exxon Corp. v. Wyoming State Board of Equalization*, 783 P.2d 685 (Wy. 1989), that a

taxable use occurs for use tax purposes only when the subject property is used in the manner "for which it was designed, constructed or intended . . . ." *Exxon Corp.*, 783 P.2d at 688.

In *Exxon Corp.*, Exxon purchased pipe from a Texas vendor that it intended to install in Wyoming. The pipe was first delivered to Colorado, where it was sandblasted, coated with epoxy, and otherwise prepared for use. The pipe was then installed in Wyoming.

Wyoming levies a use tax on the "first use" of property in that state.[2] Wyoming assessed Exxon for use tax on the pipe, claiming that the preparation work performed on the pipe in Colorado was not a use of the property for use tax purposes, and consequently that the first use was in Wyoming. The Wyoming Supreme Court agreed.

> The activities in Colorado were merely processes necessary to prepare the pipe for the use intended, i.e., its installation into and ultimate use as part of the Shute Creek CO[2] pipeline in Wyoming. The Board properly concluded that it is a use of the property in the manner for which it was designed, constructed or intended that constitutes "first use" as that phrase was intended by the Wyoming Tax Commission in Chap. IV, §3. When making the determination as to whether the first use of the property occurred in Wyoming or another state, the Tax Commission looks to the nature of the property, its intended use, and whether the property was actually used in that manner in the other state. We hold that the Board properly found that the first use in this case was the incorporation of the pipe into the Shute Creek CO[2] pipeline.

Exxon Corp., 783 P.2d at 688.

The components in issue were designed, constructed, and intended for use at the customers' out-of-state job sites. The incidental preparation work performed

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[2]There is no substantive difference between a "use" of property for Alabama use tax purposes, and a "first use" under Wyoming law.

on the materials by C&S in Alabama was not a use of the components for their intended purpose, and thus was not a taxable use for Alabama use tax purposes.[3] Consequently, the temporary storage exclusion applied, and the components installed outside of Alabama were not subject to Alabama tax.

The temporary storage exclusion also applies for local tax purposes. See, Code of Ala. 1975, §11-51-204 and Dept. Reg. 810-6-5-.23(6) (Local governing bodies must comply with all Department regulations relating to like-kind taxes.). Local use tax (not sales tax) would thus be due, if applicable, in the counties and municipalities in Alabama in which the components were installed. In that regard, C&S Components properly paid local tax in Alabama. The taxable measure, however, would be the cost of the materials only.

The Department is directed to recompute C&S Components' State and City of Clanton liabilities as indicated above. A Final Order will then be entered. As suggested by the Department, C&S Components may also file joint refund petitions with its customers for any local taxes previously overpaid.

This Opinion and Preliminary Order is not an appealable Order. The Final Order, when entered, may be appealed to circuit court within 30 days. Code of Ala. 1975, §40-2A-9(g).

Entered February 15, 2002.

[3]To my knowledge, the Department has never attempted to assess use tax on property that was only being prepared for its intended purpose in Alabama, but was subsequently used for that purpose outside of Alabama. The Department also did not argue in this case that the preparation work performed on the components in Clanton constituted a taxable use of the components.