

**New York State Department of Taxation and Finance  
Office of Tax Policy Analysis  
Technical Services Division**

TSB-A-00(11)S  
Sales Tax  
February 29, 2000

STATE OF NEW YORK  
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S990608A

On June 8, 1999, the Department of Taxation and Finance received a Petition for Advisory Opinion from Northrop Grumman Corporation, Tax Department, A12-025, South Oyster Bay Road, Bethpage, NY 11714. Petitioner, Northrop Grumman Corporation, provided additional information pertaining to the Petition on June 16, 1999 and on June 25, 1999.

The issue raised by Petitioner is whether its purchases of repair items and services used in the performance of its caretaker maintenance contracts with the United States Government are subject to sales and compensating use tax.

Petitioner submitted the following facts as the basis for this Advisory Opinion.

Petitioner designs, develops and manufactures aircraft and aircraft subassemblies. Much of its work is done under United States Government contracts. In the past, when it was fully operational, the United States naval facility located in Calverton, New York, was the site of final assembly and testing by Petitioner of large aircraft parts manufactured for the Department of the Navy (Navy). Today, the Calverton plant is basically vacant, and Petitioner has entered into a contractual agreement with the Navy to maintain the facility by providing all of the services and supplies needed to preserve the property and keep it in a full state of readiness. The facility consists of land, buildings and a runway, all of which are wholly owned by the Navy.

Petitioner has a similar contract with the Navy for a portion of the naval facility at Bethpage, NY, and has submitted a copy of this contract for "Caretaker Maintenance at the Naval Industrial Reserve Plant # 464, Bethpage, New York" as part of its Petition. The contract describes the Bethpage facility as a "Government Owned Contractor Operated (GOCO) complex." Unlike Calverton, the Bethpage facility is Petitioner's fully operational "program site" which houses the accounting, engineering, laboratory, human resource and research and development divisions of Petitioner's aircraft manufacturing business. Petitioner employs approximately twenty-three hundred people here. Also unlike Calverton, Petitioner owns most of the land and buildings located at the Bethpage plant, and what property it does not own it leases from the Navy.

Petitioner's contract for the Bethpage facility calls for it to provide services to operate, maintain, preserve and protect the facility. This includes security services, general maintenance of grounds and buildings, grass cutting, window repair, maintenance of outside and inside lighting, plumbing, electrical connections, heating and cooling systems, pest control, waste disposal, painting and anything else necessary to maintain the facility in proper working order. It also includes operation of the facility's boilers and heating systems, water distribution and electrical distribution

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systems, and fuel oil and utilities procurement to ensure the continuous operation of the systems/equipment and to satisfy the demand and consumption requirements of caretaker operations.

In Petitioner's performance of its contracts for both the Calverton and Bethpage facilities, certain services are performed by Petitioner's employees and others are subcontracted out to third parties. When Petitioner buys supplies such as light bulbs, fuel, wiring and other repair items, and services such as electricity, security service, or repair service, which are required for Petitioner to perform services under the contracts, Petitioner makes such purchases in its own name and pays its supplier or service provider for the goods or services. Petitioner then submits vouchers to the Navy to be reimbursed for its expenses. In cases where work is subcontracted out, the subcontract is between Petitioner and the third party; and the Navy is not a party to such a subcontract.

Petitioner's contracts are cost plus fixed fee contracts where the fixed fees cannot change. Costs incurred by Petitioner in the performance of the contracts are reimbursed by the government. If the negotiated cost is exceeded, it must be renegotiated. The fixed fee represents Petitioner's profit.

### **Applicable Law and Regulations**

Section 1105 of the Tax Law provides, in part:

**Imposition of sales tax.** — . . . there is hereby imposed and there shall be paid a tax . . . upon:

(a) The receipts from every retail sale of tangible personal property, except as otherwise provided in this article.

(b) The receipts from every sale, other than sales for resale, of gas, electricity, refrigeration and steam, and gas, electric, refrigeration and steam service of whatever nature. . . .

(c) The receipts from every sale, except for resale, of the following services:

\* \* \*

(5) Maintaining, servicing or repairing real property, property or land, as such terms are defined in the real property tax law, whether the services are performed in or outside of a building. . . .

\* \* \*

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(8) Protective and detective services, including, but not limited to, all services provided by or through alarm or protective systems of every nature, including, but not limited to, protection against burglary, theft, fire, water damage or any malfunction of industrial processes or any other malfunction of or damage to property or injury to persons, detective agencies, armored car services and guard, patrol and watchman services of every nature other than the performance of such services by a port watchman licensed by the waterfront commission of New York harbor, whether or not tangible personal property is transferred in conjunction therewith.

Section 1115(a) of the Tax Law exempts from the sales tax imposed by Section 1105(a) of the Tax Law and from the compensating use tax imposed under Section 1110:

\* \* \*

(16) Tangible personal property sold to a contractor, subcontractor or repairman for use in maintaining, servicing or repairing real property, property or land of an organization described in subdivision (a) of section eleven hundred sixteen, as the terms real property, property or land are defined in the real property tax law; provided, however, no exemption shall exist under this paragraph unless such tangible personal property is to become an integral component part of such structure, building or real property.

Section 1116(a) of the Tax Law provides, in part:

Except as otherwise provided in this section, any sale or amusement charge by or to any of the following or any use or occupancy by any of the following shall not be subject to the sales and compensating use taxes imposed under this article:

\* \* \*

(2) The United States of America, and any of its agencies and instrumentalities, insofar as it is immune from taxation where it is the purchaser, user or consumer. . . .

Section 528.17 of the Sales and Use Tax Regulations provides:

Tangible personal property sold to a contractor, subcontractor or repairman for use in maintaining, servicing or repairing real property of an organization described in Part 529 of this Title is exempt if it is to become an integral component part of such structure, building or real property.

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*Example:* A painting contractor uses masking tape on a contract for an organization described in Part 529 of this Title. The tape is subject to tax since it will not become an integral component part of the real property.

Part 529 of the Sales and Use Tax Regulations provides, in part, for exemption from sales and compensating use taxes with respect to the United States of America and any of its agencies and instrumentalities.

Section 541.2(c) of the Sales and Use Tax Regulations defines *agency contract* as:

. . . an agreement which permits a contractor and subcontractor to act as an agent of, that is, in the place of the principal, his customer. Purchases made by the agent-contractor or agent-subcontractor on behalf of the principal are treated in the same manner as if the purchases were made by the principal. All purchases (including rentals of contractor's tools, supplies, machinery and equipment) made by the agent-contractor or agent-subcontractor on behalf of the principal are treated in the same manner as if the purchases were made by the principal.

Section 541.3 of the Sales and Use Tax Regulations provides, in part:

(d) *Contracts with exempt organizations.* (1) Tangible personal property incorporated into real property owned by a governmental entity or by an exempt organization is exempt, whether the contract is on a lump sum, time and material, cost-plus, or other basis.

(2) Purchase for contracts (other than agency contracts).

(i) Tangible personal property sold to a contractor, subcontractor, or repairman for use in erecting, repairing, adding to, or altering a structure or building owned by an exempt organization, described in section 1116(a) of the Tax Law, is exempt when it is to become an integral component part of such structure or building.

\* \* \*

(ii) Purchases of tangible personal property incorporated into the real property of an exempt organization by subcontractors and repairmen are accorded the same treatment as purchases by the prime contractor.

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(iv) Except for agency contracts, contractors' purchases of construction supplies which do not become part of an exempt organization's real property and are used or consumed by the contractor, as well as purchases of taxable services, such as electricity used by the contractor, are subject to tax.

The following types of property and services are representative, but not intended to be all-inclusive, of contractor's purchases which are subject to tax, irrespective of whether the contractor has a time and material, lump sum, or other type of contract (except agency contract), with an exempt organization:

- (a) construction machinery and equipment, including rentals and repair parts;
- (b) contractors' office supplies;
- (c) contractors' supplies, tools, and miscellaneous equipment, whether purchased or rented, including materials to make forms and scaffolding;
- (d) any other items purchased or rented by a contractor for his use in performing the contract and not incorporated into the realty. (Emphasis added)

### **Opinion**

Petitioner has entered into contracts with the Navy to provide caretaker services for certain naval facilities which include land, buildings and a runway. Section 1116(a)(2) of the Tax Law designates agencies and instrumentalities of the United States of America as exempt organizations exempt from the payment of sales tax. The Navy is an agency of the United States and is therefore exempt from direct taxation on its purchases. Purchases of materials and services by a contractor for use in performing a maintenance contract for an exempt organization are not exempt merely because the contractor has an agreement with the exempt organization. Purchases for such a contract are exempt from sales and use taxes only if the property and services are purchased by the contractor or subcontractor as agent for the exempt organization, or if some statutory exemption applies, such as Section 1115(a)(16) of the Tax Law which exempts tangible personal property purchased by a contractor that is used to perform repair services to the exempt organization's real property, if the tangible personal property is actually incorporated into (becomes part of) the real property of the exempt organization (see Village of East Aurora, Adv Op Comm T&F, April 8, 1999, TSB-A-99(24)S).

Petitioner's purchases, therefore, of tangible personal property for use in repairing or maintaining the naval facilities, which do not become part of the facilities, are subject to sales and compensating use taxes, as are Petitioner's purchases of services contemplated under the contracts, unless Petitioner makes such purchases as the government's agent. In Matter of MGK Constructors,

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Dec Tax App Trib, March 5, 1992, TSB-D-92(23)S, the Tribunal held that since no regulation sets forth criteria for establishing whether an agency relationship exists with an exempt organization identified in Section 1116(a)(2) of the Tax Law, the general rule of agency as cited in Matter of Hooper Holmes v Wetzler, 152 AD2d 871, lv den, 75 NY2d 706, must be applied. In that decision, the court stated “to establish an agency or representative relationship there must be a manifestation that petitioners consented to act as agent on behalf of their clients, subject to the latter’s control, and that the clients authorized this fiduciary relationship.”

Applying this principle in Petitioner’s case, several factors lead to the conclusion that there is no agency relationship between Petitioner and the United States Government. The Caretaker Maintenance Contract submitted by Petitioner does not contain any language which expressly confers agency status on Petitioner; nor does the contract provide that Petitioner accepts its status as such an agent. It does not provide that Petitioner is to act as the purchasing agent of the government, nor is the government obligated to the vendors for the purchase price of the property or service purchased, which factors were found significant for the establishment of an agency relationship in Kern-Limerick v. Scurlock (347 US 110). Rather, it is Petitioner’s credit, not the credit of the government, that is bound on the purchases, as purchase orders are in Petitioner’s name and the purchase orders do not provide that purchases are being made by the government. Petitioner advances its own funds to pay vendors and subcontractors, and then must submit vouchers, invoices and supporting documentation to the government to obtain reimbursements of its costs. These elements indicate a lack of consent by the government and Petitioner to create an agency relationship with respect to Petitioner’s purchases (see Matter of West Valley Nuclear Services Co., Inc., Dec Tax App Trib, November 13, 1998, TSB-D-97(37)S). Therefore, it cannot be shown that Petitioner is acting on behalf of the United States government as its purchasing agent, subject to the government’s control, and that the government has authorized this fiduciary relationship. Thus, Petitioner’s purchases are not exempt on the basis that it is acting as an agent for an exempt organization under Section 1116(a)(2) of the Tax Law.

Petitioner, rather than the government, is making the purchases required under the contracts. Sales of tangible personal property to Petitioner, as a contractor, for use in performing its caretaker services, are retail sales as defined under Section 1101(b)(4)(i) of the Tax Law, subject to the tax imposed under Section 1105(a) or 1110 of the Tax Law. Accordingly, Petitioner must pay sales or use tax on its purchase or use of such property. However, under the provisions of Section 1115(a)(16) of the Tax Law, Petitioner may purchase tangible personal property which it uses to maintain or repair Navy owned property, provided that the tangible personal property is incorporated as an integral component part of a structure, building or real property owned by the Navy. For example, Petitioner could purchase exempt from tax paint or spackling used for painting, window parts, wiring, and certain electrical, heating, cooling and plumbing apparatus, provided that such items become an integral component part of Navy realty. See Section 528.17 of the Sales and Use Tax Regulations. See also Bedford Hills Supply, Inc., Adv Op Comm T&F, July 23, 1997, TSB-A-97(46)S. When purchasing the qualifying property from a supplier, Petitioner or its

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subcontractor must issue Form ST-120.1, *Contractors Exempt Purchase Certificate*, to the supplier within 90 days after delivery of the property. See Section 1132(c) of the Tax Law and Section 541.3(d)(2)(v) of the Sales and Use Tax Regulations.

Supplies purchased by Petitioner are not considered to become an integral component part of the government's real property. Supplies are considered to be used or consumed by Petitioner in the performance of its contracts. No tax exemption applies to supplies purchased for Petitioner's own use. Therefore, Petitioner must pay tax on paint brushes, drop cloths, grass cutting supplies, light bulbs, fuel and any other items purchased for use in complying with its contractual obligations which are not incorporated into the realty of the Navy (see Suffolk County Department of Parks, Adv Op Comm T&F, July 11, 1994, TSB-A-94(29)S; Sullivan Humes Painting, Adv Op Comm T&F, August 31, 1987, TSB-A-87(31)S; Bedford Hills Supply, Inc., *supra*).

Likewise, Petitioner's purchases of taxable services for use in complying with its contractual obligations, such as electric, utility, pest control, waste disposal or guard services, are subject to tax. These services are used by Petitioner in the completion of its contracts. Since Petitioner is the purchaser-consumer of these services, Petitioner cannot purchase them for resale and they are subject to tax (West Valley Nuclear Services Co., Inc., *supra*; MGK Constructors, *supra*).

DATED: February 29, 2000

/s/

John W. Bartlett  
Deputy Director  
Technical Services Division

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.