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October 6, 1993

BURTON W. OLIVER
Executive Director

Ms. C--- Y. C---
Certified Public Accountant
XXXXX --- ---
---, CA XXXXX

Dear Ms. C---:

This is in response to your letter of July 6, 1993. You ask how sales or use tax applies when inventory is purchased in California or out-of-state, and thereafter shipped outside California.

Your first scenario is:

“Corporation A purchases most of its inventory from California vendors and has warehouses in California. Occasionally, Corporation A would withdraw inventory from its warehouses for internal use in its sales offices outside California or ship the products as promotional gifts to its customers outside California. The issue here is whether the withdrawal of inventory which are purchased from California vendors and shipped outside the state for use are subject to California use tax.”

We assume that the corporation is a retailer engaged in the business of selling or leasing tangible personal property in this state. The corporation is therefore required to obtain a California seller’s permit. (Rev. & Tax. Code § 6066.)

Sales tax is imposed on all retailers measured by their gross receipts from retail sales of tangible personal property in this state. (Rev. & Tax. Code § 6051.) When the sales tax does not apply, use tax is imposed on the sales price of property purchased from a retailer for use, storage, or other consumption in California. (Rev. & Tax. Code §§ 6201, 6204.)

Since you indicate that the property in question is inventory, we assume that the corporation purchased the property ex-tax for resale by issuing resale certificates to its vendors. (Reg. 1668.) Further, we assume that the corporation properly issued such certificates. That is, we assume that when the corporation purchased the property it intended to resell it.

If a purchaser who gives a resale certificate thereafter makes any use of the property other than retention, demonstration, or display while holding it for sale in the regular course of business, the purchaser owes use tax measured by the purchase price. (Rev. & Tax. Code. § 6094.) Use is defined in Revenue and Taxation Code section 6009 as exercising any right or power incident to ownership, except sale in the regular course of business.

In your letter, you concluded that the corporation's promotional gifts shipped to recipients outside California and shipments for internal use should accrue use tax based on the state where the products are shipped, relying on Regulation 1620(b)(5), which states in part:

“‘Storage’ and ‘use’ do not include the keeping, retaining or exercising any right or power over property for the purpose of subsequently transporting it outside the state for use thereafter solely outside the state,....”

A donor of property uses that property by giving it away. (Reg. 1670.) The sale of the property to the donor, or the donor's use of the property in California is subject to sales or use tax. When the donor transfers property to a common carrier in California for shipment to a donee outside California, that donor has consumed the property in California. At that time, the donor has made all the use of that property that it ever will; that is, it has given up all power incident to ownership. Thus, Corporation A consumes property at the time it transfers that property to a common carrier for shipment out-of-state to its clients as promotional gifts. Since Corporation A transfers the property to a carrier in California for shipment out-of-state as gifts, its use or consumption takes place in California, and that California use is subject to California use tax. Because Corporation A uses the property in California, Regulation 1620(b)(5) is not applicable. There is no exception on account of a subsequent shipment of the property outside California. (BTLG Ann. 280.0360.)

Unlike the property Corporation A gives to its clients, when Corporation A ships property to its own offices, title does not pass to another person when it transfers the property to the carrier. Corporation A retains its right or power over the property, incident to ownership, since it is shipping the property to itself and retains title. Thus, the property Corporation A withdraws from its inventory for shipment to its out-of-state offices for internal use is not consumed or used in California. Based on the assumption above that Corporation A did not avoid paying sales tax reimbursement by issuing a resale certificate when it knew that it would use certain property, it would not be liable for use tax with respect to the property it ships to its out-of-state offices for use out of state.

I note you have expressed concern that Corporation A may have to pay tax to California and again to the state where the property is shipped. If the corporation were to pay tax to another state and subsequently used the property in California and were taxed in California, a credit would be allowed against that tax not to exceed the tax imposed in this state. (Tax. & Rev. Code § 6406.) Other states have similar provisions. Since the incidence of California tax, if applicable, would occur prior to any incidence of another state's tax, the California credit provision is inapplicable, but the other state's provision may apply.

Your second scenario is:

“Inventory purchased from out of state vendors and subsequently transported by Corporation A outside the state either for internal use in its sales offices or promotional type products for its customers. The issue here is whether the withdrawal of inventory which are purchased from out of state vendors and subsequently shipped outside the state for internal use or free promotional gifts are subject to California use tax.”

The only difference between this scenario and your first one relates to property purchased from out-of-state vendors. Even though corporation knows that it will use certain property and will not resell it, “use” for purposes of California Sales and Use Tax Law does not include storage of tangible personal property for the purpose of subsequently transporting it outside California for use solely outside California. (Rev. & Tax. Code § 6009.1.) Thus, as long as corporation makes no use of the property in California, California use tax would not apply. However, corporation would still be regarded as making a taxable use of property in California when it gives property as gifts and delivers it to a carrier in California for shipment outside this state.

If we can answer any other questions, please feel free to write again.

Sincerely,

Rachel M. Aragon
Staff Counsel

RMA:ljt