

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION

**330.1878**

In the Matter of the Claim for	)	DECISION AND RECOMMENDATION
Refund Under the Sales and Use	)	
Tax Law of:	)	
	)	
E--- H--- & R--- S---	)	No. SR -- XX XXXXXXX-001
ET AL.	)	
dba F--- F--- SERVICES - O---	)	
	)	
<u>Petitioner</u>	)	

The preliminary hearing on the above taxpayer's claim for refund was waived. James E. Mahler, Hearing Officer.

Subject of Claim

Claimant seeks a refund in an unspecified amount. The taxes were paid after an audit and reaudit for the period September 1, 1980, through December 31, 1983, which included the following audit items:

<u>Item</u>	<u>State, Local and County</u>
A. Lease receipts not reported	\$ 67,427
C. Assignments of leases with transfer of title	\$169,441

Taxpayer's Contentions

1. Tax was paid to the vendor on several transactions.
2. The assignments of leases to financial institutions did not entail sales of the leased property

Summary

Claimant is a partnership engaged in the "finance lease" business. As we understand it, the customers in these transactions normally negotiate to purchase tangible personal property from suppliers but come to claimant in order to obtain financing. Claimant purchases the property in its own name, pursuant to the price and other terms as negotiated by the customers

and then leases the property to the customers. Insofar as concerns us here, none of the leases involved mobile transportation equipment or other types of property subject to exclusion under Revenue and Taxation Code Section 6010(e)(1) to (e)(4).

1. Sometimes claimant buys the property tax-paid and sometimes it does not. Claimant contends that it paid tax reimbursement to the vendor or use tax to the state in some cases where the audit found to the contrary. No evidence has been presented.

2. In order to obtain financing to purchase the property, claimant often assigns the leases to a financial institution. The audit found that the assignments to the following financial institutions were accompanied by sales of the leased property: C--- Thrift, A--- Thrift & Loan Assn., C--- Thrift & Loan and C--- F--- Corporation (later W--- C--- M---). In cases where the underlying lease was not a sale or purchase, the audit further found that the sale of the leased property was subject to tax. Tax was asserted on the gross receipts from the sale, less a tax-paid purchases resold deduction where appropriate.

The finding that claimant had sold the leased property was based exclusively on the language of the lease assignment contracts. Specifically, the audit found that the following contractual language evidenced an intent to pass title from claimant to the financial institution.

The contracts with C--- Thrift and A--- Thrift & Loan Assn. provided:

“For value received, [claimant] hereby assigns to [the financial institution] the annexed lease of personalty.... As security of payment for rents, [claimant] also assigns all right, title, and interest of lessor in and to the personalty leased....”

The contracts with C--- Thrift and Loan and C--- F--- Corporation (W--- C--- M---) provided:

“As an inducement to extend or continue credit to [claimant], but without obligation to do so, [claimant] sells, transfers and assigns to [the financial institution] (hereafter called “lender”) all its right, title and interest in and to the lease...[¶] To secure lessee’s payments, [claimant] hereby transfers to lender a security interest in...the leased equipment....”

Some financial institutions refused to deal directly with claimant. In such cases, claimant assigned the leases to a corporation called F--- L--- Consultants, Inc. (FLC), and FLC then assigned the leases to the financial institution. The audit found that the assignments from claimant to FLC were accompanied by sales of the leased property. Tax was asserted in the manner described above.

The contracts between claimant and FLC provided:

“For value received, [claimant] hereby sells, assigns, transfers and sets over to [FLC] all of its rights, title and interest (a) in and to the [lease] agreement...and (c) in and to the property described in said agreement.”

Claimant refers to FLC as the “managing corporation” for claimant and various other partnerships. However, we are uncertain as to whether there is any common ownership or other legal relationship between FLC and claimant.

### Analysis and Conclusions

1. No evidence has been presented to indicate that claimant paid tax reimbursement or use tax on any transaction where the audit found to the contrary. Accordingly, we recommend no adjustment.

2. Sales and Use Tax Regulation 1660 provides, in the second paragraph of subdivision (c)(9)(A):

“Generally, when an existing lease that is not a ‘sale’ and ‘purchase’ is assigned, whether or not title to the leased property is transferred, the rental payments are not subject to tax. If title is transferred, tax applies measured by the sales price.”

We have reviewed the assignment contracts between claimant and C--- Thrift, A--- Thrift & Loan Assn., C--- Thrift & Loan and C--- F--- Corporation (W--- C--- M---). We agree with claimant that the language of these documents does not evidence an intent to transfer title. The documents are phrased in terms of a grant of a security interest, with no passage of title unless and until such time as the contract might be breached.

This does not end our inquiry, however. “In sales and use tax matters, the language used by the parties to characterize their transaction does not, in itself, necessarily control.” (Southern California Edison Co. v. State Board of Equalization, 7 Cal.3d 652, 662; see also Cedars-Sinai Medical Center v. State Board of Equalization, 162 Cal.App.3d 112.) Therefore, despite the language of the contracts, we would conclude that a taxable sale occurred if other evidence indicated that title in fact passed from claimant to the financial institution.

Such other evidence would include the following factors: (1) Whether claimant or the financial institution retained title in the property after the payments to the financial institutions were completed; (2) Whether the parties filed financing statements under the Uniform Commercial Code; (3) Whether the parties treated the transaction as a sale or a loan for income tax purposes, and more specifically, whether claimant or the financial institution claimed depreciation, investment tax credits or similar deductions predicated upon ownership of the property; and (4) Whether the putative interest rate, if the transaction were treated as a loan, would be usurious under California Law.

No such evidence has been presented, however. Lacking such evidence, we conclude that title in the property did not pass from claimant to the financial institutions. Accordingly, these transactions were not taxable sales.

We reach a different conclusion with respect to the transactions between claimant and FLC, however. The documentation for these transactions expressly stated that title would pass from claimant to FLC. As above, the language of the documents would not necessarily be controlling, if contrary evidence were presented but no such contrary evidence is available. Accordingly, for these transactions, we find that title did pass and that a taxable sale occurred.

Claimant waived appearance at the preliminary hearing on the assumption that sufficient evidence had already been presented to warrant a decision in its favor. Since we have found the evidence insufficient with respect to the transactions with FLC, claimant should be given an opportunity to present further evidence. We recommend that the record in this matter be held open for 30 days for that purpose.

Recommendation

Grant the claim with respect to the transactions with C--- Thrift, A--- Thrift & Loan Assn., C--- Thrift & Loan and C--- F--- Corporation (W--- C--- M---). Hold the record open for 30 days so that claimant may present additional evidence with respect to the transactions with FLC. Necessary computations are to be initiated by \_\_\_\_\_.

\_\_\_\_\_  
James E. Mahler, Hearing Officer

1/16/87  
\_\_\_\_\_  
Date

REVIEWED FOR AUDIT:

\_\_\_\_\_  
Principal Tax Auditor

\_\_\_\_\_  
Date