STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
450 N STREET, SACRAMENTO, CALIFORNIA
(PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082)
TELEPHONE (916) 322-2976
FAX (916) 323-3387

August 29, 1996

Mr. D--- B. F---, Manager
Multistate Tax Services
--- & --- L.L.P.
XXX --- ---, Suite XXXX
---, CA XXXXX-XXXX

Re: H--- & S--- H--- Corporation
SY --- XX-XXXXXX

Dear Mr. F---:

This is in response to your letter dated June 20, 1996 in which you state:

"Thank you for your response of May 30, 1996 to our inquiry regarding the application of California Sales and Use Taxes to the above-referenced client's purchase of the assets of two companies engaged in the business of selling bottled water and leasing water coolers. Your response was very informative and provided us guidance in advising our client with respect to its California Sales and Use Tax obligations.

"As we discussed in our telephone conversation of June 10, however, there remain a couple of questions for which we would appreciate additional clarification."

"Scenario 1 - Transactions Are Occasional Sales

"We discussed the possibility of the transactions ultimately being held to be exempt occasional sales and we agreed the possibility was remote, at best. Nonetheless, for the sake of clarification, could you please answer the following question:

"In the event the transactions were found to be exempt occasional sales, is there any provision in the law that the water coolers, sold subject to leases which are not continuing sales, would not qualify for the exemption? That is, would

H&S be required to pay use tax on the purchase price of the water coolers even though it were an occasional sale and even though it would not have a right to elect to pay tax measured by rental receipts?

"Scenario 2 - Transactions Are Not Occasional Sales

"Based on the facts presented in our inquiry, you concluded that the sales of the assets at issue were taxable retail sales, including the sales of tax-paid water coolers subject to leases which were not continuing sales. Our understanding is that the transactions would be subject to sales tax and that the obligation of the purchaser to reimburse the seller for its tax liability is governed by the contract of sale in accordance with Civil Code section 1656.1 (Pursuant to the actual contract of sale in our transaction, any sales tax due is borne by the seller - see extract from the sales contract attached.) However, at the bottom of page 4 of your letter, you state, 'As explained above, H&S owes tax on cost.'

"If these transactions are not occasional sales but are taxable retail sales,

"A. Who is liable for the tax?

"B. If the seller is liable for the tax and pays the tax to the State Board of Equalization and does not charge the tax to the purchaser nor get reimbursed from the purchaser, does the tax-paid status of the leased equipment carry over to the purchaser?"

"...."

With respect to the facts you provided in your inquiry dated April 9, 1996 (incorporated herein by reference), I stated:

"The applicable exemption is set forth in Revenue and Taxation Code section 6367, which provides an exemption for certain occasional sales as defined in subdivision (a) of Revenue and Taxation Code section 6006.5. Section 6367 provides an exemption from tax for an "occasional sale" of tangible personal property other than vehicles, vessels, and aircraft. You state that some of the assets purchased by H&S constitute delivery vehicles. With respect to the transfer of the vehicles, the exemption set forth in section 6367 does not apply.

"Further, section 6006.5(a) defines 'occasional sale' as a sale of property not held or used by a person in the course of activities for which the person is required to hold a seller's permit. You state that the two selling companies had California seller's permits for the purpose of selling paper cups, and for making sales of taxable items under the Office Refreshment Program. The sales under the

Office Refreshment Program appear to be related to the selling companies' leases of water coolers and other related equipment. Their sales of the paper cups were clearly part of their businesses involving the leases of the water coolers. As a result of the activities in which the selling companies were involved, they were required to hold, and did in fact hold, seller's permits. Since it appears that the tangible personal property sold was used in the course of activities requiring the holding of those seller's permits, the section 6367 exemption does not apply, even with respect to property that does not constitute vehicles, without regard to the number of sales that took place within any twelve-month period.

"With respect to the leases, we assume that none of the property transferred constitutes mobile transportation equipment. As you know, a lease of tangible personal property in California is a continuing sale and purchase unless the lessor leases the property in substantially the same form as acquired and has made a timely election to pay California sales tax reimbursement or use tax measured by the lessor's purchase price of the property. (Rev. & Tax. Code §§ 6006(g)(5), 6006.1, 6010(e)(5), 6010.1, Reg. 1660(c)(2).) When a lease is a continuing sale and purchase because either or both of the foregoing conditions is not satisfied, the lease is subject to use tax measured by rentals payable. (Reg. 1660(c)(1).) The lessee owes the tax, which the lessor is required to collect from the lessee and pay to this Board. (Rev. & Tax. Code §§ 6202, 6203, 6204; Reg. 1660(c).)

"You state that all coolers were purchased by the selling companies with tax paid on cost, and that tax was not charged on rental receipts. This means that H&S purchased the coolers subject to leases which are not continuing sales. The sale to H&S is therefore a taxable retail sale, with tax measured by the sales price of the property to H&S. (Reg. 1660(c)(9)(A).)"

You ask what our analysis would be if we had found that the sales to H&S were occasional sales. As I stated in my May 30, 1996 letter to you, based on the information you provided, the sales to H&S were not occasional sales but were instead taxable retail sales.

You ask us to assume in answering your next two questions that the sales are taxable retail sales. The answers to these questions are as follows:

A. A retailer owes sales tax on its retail sales taking place in California. (Rev. & Tax. Code § 6051.) It appears from the facts you have provided that the sales to H&S occurred inside of California. Where sales tax applies, a retailer may collect reimbursement for its sales tax liability from the purchaser if the contract of sale provides for such reimbursement. (Civ. Code § 1656.1.) Therefore, the entities that sold the property to H&S owe the sales tax. If such entities have a contract right of reimbursement against H&S, then H&S owes those entities tax reimbursement on the sales price of the property to H&S.

B. You have asked whether the tax paid status of the leased equipment carries over to the purchaser. The answer to this question is no. The sale to the purchaser is a retail sale with no option to purchase the equipment for resale. (Reg. 1660 (C)(9)(A).) Thus, if the sellers pay sales tax, no further tax is due on the transactions between the sellers and the purchaser, and the question of sales tax reimbursement is a matter of contract between the sellers and the purchaser. In addition, the existing leases are still not continuing sales. However, for any future leases, sections 6006(g)(5) and 6010(e)(5) govern. Those provisions provide that a lease is a continuing sale unless the lessor has paid sales tax reimbursement or use tax on purchase price. Since the lessor here would not have paid tax or tax reimbursement (and the seller is not a "transferor" as defined in these sections), future leases would be taxable continuing sales.

If you have further questions, please feel free to write again.

Sincerely,

Kelly W. Ching
Tax Counsel

KWC:cl

cc: Out-of-State District Administrator
Sacramento District Administrator