STATE BOARD OF EQUALIZATION

December 13, 1971

Mr. J--- G. S---
Attorney at Law
XXX --- --- St., Suite XXXX
--- ---, California XXXXX

Dear Mr. S---:

SR -- XX XXXXXX
The C--- P---, Inc.
P--- N--- Division

This is with reference to the petition of The C--- P---, Inc., P--- N--- Division, and the hearing held on the matter last October 29 in Downey, California.

Briefly, C--- P--- held a seller's permit and made retail sales of printed matter that did not qualify for sales tax exemption under Section 6362 of the Revenue and Taxation Code. The taxable sales were around 2.5 to 3.5 percent of the total sales.

C--- P--- sold its California division to the D--- P--- for $2,500,000 under an agreement that contained a breakdown of the selling price as follows: $2,320,000 for machinery and equipment and $180,000 for assignment of printing contracts. No part of the agreed upon price was allocated to goodwill, transfer of leasehold interest, etc.

The machinery and equipment consisted of four main presses and a proof press, along with supporting equipment and the office equipment necessary to operate the business.

The sale was completed on August 21, 19XX, and the D--- P--- hired the A--- A--- Company of --- to make a fair market value appraisal of the machinery and equipment acquired under the agreement using August 21, 1968 as the effective date of the values placed or assigned to the property purchased.

The appraisal valued turned out to be about $182,500 less than the selling price agreed upon. In other words, the appraised figure was $2,157,500 rather than $2,320,000.

Two presses were not included in the audited determination because it was understood that they were never used to print anything but exempt periodicals or other matter qualifying for the exemption under Section 6362. However, you contend that the sale of the other presses and supporting equipment should have been exempted on an occasional sale too.

Several theories were advanced to support your arguments for exemption:

1. You contend that the machinery and equipment was not held and used in an activity for which a seller's permit was required because they were used in the company's manufacturing activity and not its selling activity.

It appears that you are "departmentalizing" the C--- P--- business activities on the theory that a single business may have many activities some of which do not involve selling tangible personal property, and without the selling activity the others would not require the holding of a seller's permit. We disagree with this.

Manufacturing of goods for sale is inextricably tied to the selling of the goods manufactured. The court in Northwest Pacific Railroad v. State Board of Equalization (1943) 21 Cal. 2d at page 529, said:

> "While for reasons considered desirable plaintiff corporation may departmentalize its business, it cannot, by such process set up for tax purposes a distinction between the types and kinds of sales made to escape the tax aimed as all of such sales. Specific sales of a retailer cannot be segregated from the bulk of its sales and treated separately as isolated or occasional sales."

Your argument is contrary to the holding in U.S. Industries, Inc. v. State Board of Equalization (1962) 198 Cal. App. 2d 775, wherein the court held that a manufacturer who customarily made sales at retail and held a seller's permit is subject to the retail sales tax on the sale of all capital assets used in operating the business.

2. The second argument is one that is apparently made in an attempt to urge the Board that, notwithstanding the fact that a seller's permit was held, the taxable sales made in the regular course of business was very small in volume compared to the exempt sales that were regularly made and the seller's permit should be ignored.

There is no basis under the law on which such an argument can be sustained. Section 6266 of the Revenue and Taxation Code provides that every person desiring to engage in or conduct business as a seller within this State shall file with the Board an application for a permit. The C--- P--- did engage in business as a seller, and it made taxable as well as exempt sales.

3. The third point argued was that tax should not apply to the sale of the tangible personal property that the purchaser shipped to Denver and to the property that was not needed and which was given away after acquired. There is no basis in law that would dictate such a conclusion.

4. Notwithstanding the various arguments for deleting some or all of the items sold, you contend that the appraisal value should control over the actual price stipulated as having been paid for the machinery and equipment. This argument fails in the face of what the court held in Hawley v. Johnson (1943) 58 Cal. App. 2d 232, wherein the court held that the value fixed by agreement between seller and buyer of property exchanged as part of the purchase price, rather than the appraised or market value, constitutes "gross receipts" upon which the tax is imposed.

There is no basis on which to assume that the difference between the appraised price and the actual price agreed upon represents something paid for goodwill. There may have been goodwill and other intangibles sold along with the entire business; however, no value was, in fact, placed on the intangibles if there were any other than the assignment of printing contracts.

5. You also argue that the sale of the machinery and equipment was not one of a series of sales sufficient in number, scope, and character to constitute an activity requiring a seller's permit. Presumably, this argument is made in conjunction with the argument that the activity of manufacturing was not one, in and of itself, that required holding a seller's permit.

The liability has not been assessed on the number, scope, and character of sales of machinery and equipment made by C--- [P---]. It is asserted because the equipment was held and used in an activity for which a seller's permit was held. If the C--- P--- business activity did not involve any selling activity, it would not have needed a seller's permit and if this were so, the number, scope, and character test would have been applied.

6. Finally, it was contended that the office furniture and equipment was not held in the course of an activity requiring the holding of a seller's permit because it was not held for resale and none had been previously sold. It was sold only as a part of a sale of the entire business in a single transaction and not a series of sales. Again, this argument does not stand up in the face of the case law under U.S. Industries, Inc. v. State Board of Equalization, supra.

In summary, it is our opinion that the sale to the D--- P--- did not qualify for an occasional sale under Section 6006.5, subsection (a).

Further, it is our opinion that the proper measure of tax was the agreed upon selling price, not the appraised market value. Accordingly, we propose to recommend that the matter be redetermined without any adjustment to the audited measure of the tax.

It is noted that you have requested a hearing before the Board. Under the law, your client is entitled to such a hearing. However, if after considering our recommendation and the reasons for it, a hearing is no longer desired, please sign and return two of the three waiver of hearing forms enclosed. The third is for your records. If a hearing is still desired, the matter will be place on the Board's hearing calendar as soon as possible.

Very truly yours,

Robert H. Anderson
Tax Counsel

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Enclosures