



STATE BOARD OF EQUALIZATION

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November 9, 1993

BURTON W. OLIVER
Executive Director

P--- M---, President
T--- S--- C---
XXXX --- Avenue
---, CA XXXXX

Re: SR -- XX-XXXXXX

Dear Mr. M---:

This is in response to your letter regarding the application of sales tax to the sale of a business. Initially, I note that you ask for advice pursuant to Revenue and Taxation Code section 6596. That section provides the Board with the only basis to relieve a person for relying on incorrect advice from the Board. Section 6596 applies when a person reasonably relies on incorrect written advice from the Board in response to a written request for advice that includes all relevant facts. Your situation cannot come within section 6596 since the transaction has already occurred and the time for making a timely return has passed. You explain:

"On March 3, 1993, TSC [T--- S--- C---] sold substantially all its assets to B--- N---, Inc., a Delaware corporation ('B---')

"Prior to the Asset Sale, TSC operated a service business which stored records, corporate documents and any other boxed papers for its clients. TSC charged its clients for its services by assessing monthly storage charges per box, grossing revenues of approximately \$XXX,000 in 1991 and \$X,XXX,000 in 1992 as evidenced by the enclosed tax returns.

"As a courtesy, and on a very limited basis, TSC would sell storage boxes to certain of its clients on request. Although, TSC obtained its resale permit to offer this service, TSC's box sales from October 1991 through March 1993 totaled \$XX,579.00 (as evidenced by the enclosed sales tax returns), or approximately one (1%) percent of TSC's gross revenues.

"In the Asset Sale, 400 storage boxes with a de minimis value of approximately \$288.00 were sold to B--- with TSC's other assets."

You believe the sale is an exempt occasional sale and you cite the case of Ontario Community Foundation, Inc. v. State Board of Equalization (1984) 35 Cal.3d 811. You argue:

"TSC, as described above, also held a resale permit to accommodate its customers by making a minimal number of taxable sales, an activity wholly incidental to its service business. Therefore, as held in Ontario, it would be grossly unfair to assess sales tax against the entire Asset Sale proceeds. Accordingly, as set forth in Regulation 1595 (a) (5), the only Asset Sale proceeds subject to sales tax are those directly attributable to the sale of the tangible personal property, the 400 storage boxes with a value of \$228.00, used in the selling activity."

After the decision in Ontario Community Foundation, the Board amended Regulation 1595 to conform with that decision. The relevant provisions are as follows:

"(a) ACTIVITIES REQUIRING SELLER'S PERMIT.

"(1) GENERAL. Tax applies to all retail sales of tangible personal property including capital assets whether sold in one transaction or in a series of sales, held or used by the seller in the course of an activity or activities for which a seller's permit or permits is required or would be required if the activity or activities were conducted in this state....

"Generally, a person who makes three or more sales for substantial amounts in a period of 12 months is required to hold a seller's permit. A person who makes a substantial number of sales for relatively small amounts is also required to hold a seller's permit.

"Tax does not apply to a sale of property held or used in the course of an activity not requiring the holding of a seller's permit unless the sale is one of a series of sales sufficient in number, scope and character to constitute an activity for which the seller is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state. If tangible personal property is leased under a lease which is a 'sale' as defined in Section 6006 or a 'purchase' as defined in Section 6010, tax applies to the lease as provided in Regulation 1660. The lessor is making a 'continuing sale' which is not an 'occasional sale'.

"(2) PROPERTY HELD OR USED IN AN ACTIVITY, OR ACTIVITIES REQUIRING THE HOLDING OF A SELLER'S PERMIT. A seller's permit is required of a person engaged in the business of selling tangible personal property. The activity or activities requiring the holding of that permit include, but are not limited to, the acquisition and sale of tangible personal property at retail or for resale.

"Acquisition includes the obtaining of the property in any manner whatsoever. For example, raw materials may be purchased or may be obtained by extraction from the earth, air or waters of the earth. These may be sold in raw form or processed or manufactured into other raw materials, component parts or finished items which are sold. Each of these activities is an activity which is so related to the sale of tangible personal property, that it is part of the activity requiring holding of a seller's permit.

"(3) SEPARATE BUSINESSES. A person engaged in an activity or activities requiring the holding of a seller's permit or permits may also be engaged in entirely separate endeavors which do not require the holding of a seller's permit or permits. Tax applies to the sale of tangible personal property held or used in the course of an activity requiring the holding of a seller's permit. Tax does not apply to the sale of property held or used by the seller in the non-selling endeavors which do not require the holding of a permit. For example, a person may own a hardware store at one location and a real estate brokerage business at another location, with no relationship between the two activities except that of common ownership. Under these circumstances, a sale of furniture used in the brokerage business would not be a sale of property held or used in an activity requiring the holding of a seller's permit. A sale of tangible personal property used in the hardware business would be a sale of property held or used in an activity requiring the holding of a seller's permit.

"(4) SERIES OF SALES REQUIRING THE HOLDING OF A SELLER'S PERMIT. When a person not otherwise engaged in an activity requiring the holding of a seller's permit makes a series of sales sufficient in number, scope and character to require the holding of a seller's permit, the gross receipts from all of such sales are subject to tax.

"(A) Number. Generally the minimum number of sales to require the holding of a seller's permit is three within any 12 month period.

"(B) Scope. The extent of the sales measured by their frequency or dollar volume.

"(C) Character. This relates to the similarity in type and value giving effect to the taxpayer's operations. For example, a processor of food products for human consumption is not required to hold a seller's permit for the processing and sale of food products. Sales of used lug boxes, obsolete or used machinery, food handling and similar items are of a character that three or more sales of sufficient scope will require the processor to hold a seller's permit for this selling activity.

"(5) EXAMPLES APPLYING THE ABOVE PRINCIPLES.

"(A) Service enterprises which make some incidental sales.

"1. Operators of service enterprises such as hospitals, hotels, theaters, schools, laundromats, car washes, transportation companies, and trucking companies may make some sales incidental to their primary services business. A hospital may operate a pharmacy and cafeteria as an adjunct to the hospital. A hotel may operate a restaurant and a bar. A theater may sell popcorn to patrons. A school may operate a cafeteria and bookstore. A laundromat may sell soap to its customers.

"If any of these businesses were sold, tax would apply only to the gross receipts from the tangible personal property held or used in the selling activity.

"2. If, in any 12 month period, the operator of the service enterprise makes more than two sales in substantial amounts of tangible personal property used in the service enterprise, the gross receipts from those sales is subject to tax, unless otherwise exempt (such as a sale in interstate commerce). If one of the sales is a sale of the business, the tax applies to the gross receipts from the sale of the tangible personal property. In determining whether there are more than two sales of tangible personal property, trade-ins of used equipment for new, incidental to the service enterprise, will not be counted.

"(B) Other businesses.

"1. Tax applies to the sales of assets of a business which is not essentially a service enterprise. Examples of this are sales of grocery stores and liquor stores selling both exempt food products and taxable items, service stations which sell gasoline, oil and similar items and which also perform automotive repairs and lubrication services, pharmacies which sell exempt medicines and taxable items such as bandages and sundries.

"2. Where a service enterprise and a sales business are operated together so as to constitute one business, tax will apply to the sale of the assets of the

business. For example, if a car wash and gasoline station are operated at the same premises and the car wash is available only to persons who buy gasoline or if the price of the car wash is reduced if gasoline is purchased, tax applies to the sale of the car wash."

We agree that TSC was operating a business which, if no sales were made, would be regarded as a service business the sale of which would qualify as an exempt occasional sale. However, TSC was making sales of tangible personal property, and properly held a seller's permit with respect to such sales. The question to be answered is whether TSC's service activities were conducted in a business that can be regarded as a business separate from its sales activities. Subdivision (a)(5)(B)2. of Regulation 1595, quoted above, applies to this case. TSC presumably operated its service enterprise, the storage activities and related business (including management and billing), at the same location or locations as its sales activities. If the service activities and the sales activities were operated so as to constitute one business, then the sale of the entire business will be regarded as the sale of property used in the course of activities requiring a seller's permit.

We assume that a person could obtain storage without also purchasing the boxes, and that a person could purchase boxes without obtaining storage. We also assume that TSC did not provide storage at a lower price to a person purchasing boxes nor did it sell boxes at a lower price to a person obtaining storage. If these assumptions are correct, and if TSC made no other sales in the 12 months prior to the sale to B--- except for sales of boxes, then we believe that subdivision (a)(5)(A)1. of Regulation 1595 applies. The sale of TSC's property used in the course of its service activities (storage) would be exempt from sales tax. (Rev. & Tax. Code §§ 6006.5(b), 6367, Reg. 1595(a).) The sale of TSC's property used in the course of its sales activities are subject to tax. I note that this amount includes not simply the sales price of boxes sold at retail, but includes any amounts attributable to property used in the course of such activities, including cash registers, storage facilities for the inventory, supplies related to the sales, and any other property related to such sales.

If you have additional questions, please contact me.

Sincerely yours,

Donald L. Fillman
Staff Counsel

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