M e m o r a n d u m

415.0060

To: Mr. X----------

Date: Sept. 14, 1967

From: George A. Trigueros
Tax Counsel

This is in regard to your memo of September 6 concerning the audit of “W”. It is our understanding that "W” and "R" are two separate corporations which have the same officers and stock ownership. "R" is engaged in business as a building contractor, and "W" is engaged in the business of purchasing and selling building materials.

An audit has been made of "W" and it has been found that it has not been reporting as taxable gross receipts its markups on sales of building materials to "R". "W" contends that the amount of the markups should not be regarded as taxable gross receipts because:

1. The amounts of the markups were arbitrary.

2. The transfers are merely "intercorporate transactions".

3. The materials could just as easily have been purchased by "R” from some other building supply company, at the same price as that paid by "W".

After completion of the audit, the audit staff's attention was directed to Calif. Tax Service Annotation 1594. 20 which states:

> "Neon Signs--Selling and Leasing. Two corporations with identical officers and stock ownership, one manufacturing, selling, and installing neon signs, the other leasing and maintaining the signs, are but a single neon sign company within the meaning of Sales Tax General Bulletin 59-3 where the companies operate as a joint enterprise. Accordingly, tax applies to the cost of materials of the first company and the receipts of the second company upon the termination of the lease in accordance with the provisions of the bulletin. 7-30-64"

In view of the conclusion set forth in the annotation, the question has been raised as to whether "W" and "R" are operating as a joint adventure with respect to the sum total of their operations so that the transfer of tangible personal property between them can be deemed not to be sales under the sales tax law.

As indicated in 20 Cal. Jur. 2d, Joint Adventures, a joint adventure (venture) is an undertaking by two or more persons jointly to carry out a single business enterprise for profit. To establish the existence of a joint venture, there must be proof, as in the case of a partnership, of a community of interest and a sharing of profits and losses. Each joint venturer must have a right to direct the conduct of the other venturers through a fiduciary relation which must exist. A joint proprietary interest in the joint adventure property and joint participation in the conduct of the business are essential elements of a joint adventure.

Although two separate corporations, as persons, may form a joint adventure, the fact that the two separate corporations in question mutually derive financial benefits from transactions between themselves is not determinative as to whether they have formed a joint adventure or conducted business operations as such. On the contrary, it appears that the two corporations were formed for the business purpose of separating responsibilities for different business functions and activities between them. In view of the foregoing, it does not appear that "w" and "R" have formed or have operated as a joint adventure. Accordingly, it is our opinion that the transfer of building materials from "w" to "R" were taxable retail sales as indicated by the entries in the books of both corporations.

GAT:ph [lb]