STATE OF CALIFORNIA

557.0430

STATE BOARD OF EQUALIZATION
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September 9, 1993

Mr. R--- E---
Operations Manager
S--- & W---
G--- D--- Center
XXXX --- --- Street, Space XXX
--- ---, CA XXXXX-XXXX

Re: SY -- XX-XXXXXX

Dear Mr. E---:

This is in response to your letter of April 9, 1993, requesting our answers to your listed questions. We apologize for the delay. Although you state that the majority of your sales are for resale, your questions concern only retail sales. Your questions were as follows:

1. Are packing, crating, or freight (transportation) charges taxable?

Sales or use tax is imposed on all charges related to the retail sale of tangible personal property except those charges specifically excluded from taxation by statute. A retailer cannot avoid paying or collecting tax on part of the gross receipts from the sale of tangible personal property merely by stating some of them separately, such as overhead expenses passed through to the purchasers, unless those charges are excluded from taxation by statute. The exclusion relevant here is provided by subdivision (c)(7) of Revenue and Taxation Code Section 6012, which excludes from taxable "Gross Receipts":

> Separately stated charges for transportation from the retailer's place of business or other point from which shipment is made directly to the purchaser, but the exclusion shall not exceed a reasonable charge for transportation by facilities of the retailer or the cost to the retailer of transportation by other than facilities of the retailer; provided, that if the transportation is by facilities of the retailer, or the property is sold for a delivered price, this exclusion shall be applicable solely with respect to transportation which occurs after the sale of the property is made to the purchaser.

Charges for handling related to the sale of tangible personal property are taxable whether separately stated or not. (See Rev. & Tax. Code § 6012(a)(2): taxable gross receipts include the cost of services which are a part of the sale of tangible personal property.) Thus, a charge for "shipping and handling" is not a separate statement of shipping charges. If there is no further itemization, the charge for shipping and handling would not constitute a separate statement of transportation charges and the entire charge would be included in the measure of tax.

Although a designation "shipping and handling" is not a separate statement of transportation charges, we have considered the designation "postage and handling," coupled with a statement of the actual amount of postage placed on the package mailed to a customer, to constitute a separate statement of transportation charges excludable from the measure of tax. (Business Taxes Law Guide Annotation 557.0450 (9/16/74).) Thus, when a charge is designated as "shipping and handling," and the amount of the shipping portion paid to the carrier is clearly set forth on the package received by your customer, the amount of those shipping charges will be excludable from the measure of tax up to the amount paid by the purchaser for such shipping.

If the actual amount paid to the carrier is not clearly set forth, then the full amount of the "shipping and handling" charges would be taxable. I believe that it is becoming rare for a clear statement of the shipping charges paid to the carrier to be shown on the package. Retailers often have bulk shipping permits with carriers such as UPS, Federal Express, and the Postal Service and send their packages showing the permit number rather than the actual amount of the shipping charges. When a package is sent under such circumstances pursuant to a contract showing "shipping and handling" charges, there is no "separate statement" of transportation charges within the meaning of Revenue and Taxation Code section 6012.

The other separately stated item on your invoice is "packing." Charges for packing, crating, and other handling are taxable whether separately stated or not.

A summary of the answer to your first question is that all charges about which you inquire are included in gross receipts for tax purposes except separately stated transportation charges meeting the requirements of Revenue and Taxation Code section 6012(c)(7).

2. Would the above answer change if we made these items a profit source by adding a surcharge to our actual costs?

If you added a surcharge to packing, crating, or other handling, there would be no change: the entire handling charges are always included in your gross receipts for tax purposes. Adding a surcharge to any type of transportation charge (postage, freight, shipping) would also result in no change: transportation charges meeting the separate statement requirements discussed above are deductible, but only up to the actual transportation charge paid by the retailer to the carrier.

3. What is the tax impact of our representing out-of-state manufacturers?

There are two common business relationships that you could have with an out-of-state manufacturer, whereby it ships tangible personal property directly to the consumer in California. You could be either the retailer that has the property "drop shipped" to your customer, or you could be an agent for the manufacturer. In either case, the transaction will be subject to California taxes.

When you make a retail sale of tangible personal property, you owe the sales tax, or are required to collect the use tax, even if your supplier ships the property, per your directions, directly to your retail purchaser. If you solicit orders in California as an agent for an out-of-state company, your services in California make that out-of-state company "engaged in business in this state," and require it to collect the applicable California use tax and pay it to this state. Revenue and Taxation Code section 6203 includes, in its definition of a retailer "engaged in business in this state," the following:

> (b) Any retailer having any representative, agent, salesperson, canvasser, independent contractor, or solicitor operating in this state under the authority of the retailer or its subsidiary for the purpose of selling, delivering, installing, assembling, or the taking of orders for any tangible personal property.

The United States Supreme Court has recently clarified the criteria for determining when an out-of-state retailer may be required to collect the use tax. In Quill v. North Dakota (1992) 119 L. Ed. 2d 91, the Court held that the retailer must have a significant physical presence within the state where the property is to be stored, used, or otherwise consumed. Your physical presence in this state, as an agent acting for the retailer, results in the retailer having a physical presence in this state. This satisfies the Quill requirement.

4. Please explain our responsibilities when the products for which we invoice are components of a final product that will leave the state or are shipped to an intermediary handler.

It is presumed that all of your gross receipts are subject to sales tax until the contrary is established. (Rev. & Tax. Code § 6091.) If your contract with the purchaser requires that you ship the property to an out-of-state location and it is so shipped, by your own facilities or those of a carrier, customs broker, or forwarding agent, no sales tax will apply. If title to the property passes to the purchaser in California, the sale would nevertheless be exempt as a sale in interstate commerce. (See Regulation 1620(a)(1) and (3)(B), copy enclosed.) If title to the property passes to the purchaser outside of this state, the sales tax does not apply because the sale did not occur in California. (Rev. & Tax. Code §§ 6010.5, 6051.) If you ship to a point within the state, sales tax will apply without regard to the means of shipment, unless you receive a resale certificate.

In your first example, you ship the fabric to a California location. If this is all we know, sales tax will apply. The key factor that determines many of these cases is one of possession and

control. We assume that when you ship to Los Angeles, you lose control of the property and it could be diverted by the purchaser at any time. Regulation 1620(a)(3), which covers sales which precede movement of the property from within the state to points outside the state, provides as follows:

> **(A) To Other States--When Sales Tax Applies.** Except as otherwise provided in (B) below, sales tax applies when the property is delivered to the purchaser or the purchaser's representative in this state....
>
> **(B) Shipments Outside the State--When Sales Tax Does Not Apply.** Sales tax does not apply when the property pursuant to the contract of sale, is required to be shipped and is shipped to a point outside this state by the retailer, by means of:
>
> 1. Facilities operated by the retailer, or
> 2. Delivery by the retailer to a carrier, customs broker or forwarding agent, whether hired by the purchaser or not, for shipment to such out-of-state point

For the sale to be exempt, you must maintain possession or control of the property until you ultimately ship it to an out-of-state location pursuant to the contract terms and as specified in Regulation 1620(a)(3)(B).

It is possible to have a shipping contract which requires the carrier to ship the fabric to Hawaii with stops at the backer and upholsterer, with no opportunity for the purchaser to divert the property before it reaches Hawaii. Such a shipping contract could be arranged by the purchaser, and would qualify for the exemption, so long as, pursuant to the contract of sale, you deliver the property to the carrier for shipment to a point outside this state. (See Annotation 325.0280.)

Your second example provided that you would ship to a receiving company in Los Angeles which is packing a container for shipment to Hawaii, but that your documents only show the shipment to Los Angeles. I will assume that the Los Angeles company would qualify as a "forwarding agent" as used in Regulation 1620(a)(3)(B)2. However, since your contract fails to require delivery to such agent "for shipment to [an] out-of-state point," sales tax will apply.

If you have further questions please contact me.

Sincerely yours,

Donald L. Fillman
Tax Counsel

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Enclosure: Regulation 1620