STATE OF CALIFORNIA

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I am responding to your letter of March 31, 1994. You ask how tax applies to an automobile sales transaction you describe. You also reference Regulation 1610(d)(2). From that I assume that the transaction you are concerned about is the sale of the vehicle to you by the lessor under a lease buyout.

The facts of the transaction you describe are as follows. You purchased the vehicle and received title on March 25, 1994 when you bought out a vehicle lease at midterm. You sold the vehicle to an out-of-state buyer the same day. The vehicle was not used between March 25, 1994 and March 26, 1994. The out-of-state buyer had a trucking company pick the vehicle up at your house on March 26, 1994 and deliver it to the train station for shipment. You notified the California Department of Motor Vehicles of the sale on March 30, 1994 by submitting a signed "release of liability" form.

Retail sales of tangible personal property are subject to sales tax. (Rev. &Tax. Code § 6051.) A retail sale is a sale for any purpose other than resale in the regular course of business. (Rev. & Tax. Code § 6007.) When the sales tax does not apply, use tax applies to the use of tangible personal property purchased for use in this state. (Rev. & Tax. Code §§ 6201, 6401.) When a person purchases property and will resell that property without using it first, the sale to that person is not subject to sales or use tax.[1] Thus, if the vehicle was sold to you for resale, tax does not apply. Otherwise, tax does apply to the sale of the vehicle to you.

The initial question is whether your lease was a "true lease" or an outright sale, generally described as a "sale at inception." A contract designated as a "lease" is regarded as a sale at inception when the "lessee" is to obtain title upon completion of the required rental payments, or when the lessee has an option to purchase the property for a nominal amount, which is when the option price does not exceed $100 or one percent of the total contract price, whichever is less. (Regs. 1660(a)(2)(A).) When a lease contract is actually a sale at inception, title to the property is transferred to the purchaser at the commencement of the "lease," and there is no sale when the purchaser completes making the required payments (including the nominal option price). Sales or use tax is due in the period during which the sale occurs, that is, at the commencement of the "lease," and the full contract price of the lease (sale) is subject to tax unless the “lessor” keeps

adequate and complete records to show separately the sales price of the property and the interest, insurance, finance and carrying charges. If such records are kept by the "lessor," these charges may be deducted from the computation of the tax. (Reg. 1641(a).)

If the lease about which you inquire were actually a sale at inception, sales or use tax should have been paid to the state on the full contract price (with deductions as noted above) at the beginning of the "lease." Since there would not be another sale by the "lessor" to you at the end of the contract, no further tax would be due. You have cited Regulation 1610(d)(2) which relates to sales for resale. If the transaction were a sale at inception, Regulation 1610(d)(2) would not be applicable since the "lessor" would have sold the vehicle to you at the commencement of the "lease" and you used the vehicle prior to your sale of it. That is, your sale of the vehicle would not alter the fact that the original sale to you was subject to tax.

When a contract designated as a lease does not provide for the lessee to obtain title to the leased property after making the required payments and does not have an option for the customer to purchase the leased property for $100 or one percent of the contract price, whichever is less, the contract is a true lease. If the contract in question here were a true lease, you would not be regarded as having purchased the vehicle at the commencement of the lease. Instead, the lessor would be regarded as the owner of the vehicle unless and until you exercised an option to purchase, if any. If you exercised to an option to purchase the vehicle, you would be regarded as having purchased the vehicle at that time. If you resold the vehicle prior to making any use of it after the sale to you, then the sale to you would not be subject to tax. Regulation 1610(d) (2) is relevant to the determination of whether a person purchasing a vehicle pursuant to an option in a lease is regarded as having resold the vehicle prior to any use:

> "It will be presumed that a transfer of a vehicle to a lessee by a lessor, as defined in Section 372 of the Vehicle Code, was a sale for resale if the lessee transfers title and registration to a third party within 10 days from the date the lessee acquired title from the lessor at the expiration or termination of the lease. The presumption may be rebutted by evidence that the sale was not for resale prior to use. 'Transfer of title and registration' occurs, for purposes of this regulation, when the lessee endorses the certificate of ownership."

You do not state when you endorsed the certificate of ownership and transferred that certificate to the purchaser. I assume that you did so between March 25, 1994 and the end of the month. If your lease were a true lease, you would have transferred title to the purchaser within 10 days of having acquired title to the vehicle from the lessor, which would raise the presumption that you purchased the vehicle from the lessor for resale. The facts as stated in your letter are consistent with this presumption in that you state that you did not use the vehicle between the time you acquired title and the time you resold the vehicle.

In summary, if your contract was a sale at inception, Regulation 1610(d) (2) is inapplicable because the sale to you would have occurred at the commencement of the "lease" and you then used the vehicle before your eventual sale. Based on the information you provided, if the contract was a true lease, your purchase of the vehicle per the lease buy-out was a

nontaxable purchase for resale. We note, however, that if the latter conclusion applies, any taxes paid or due with respect to the lease (either by the lessor on its purchase price or by you on rentals payable) would have been properly due without regard to whether you are regarded as having purchased the vehicle for resale.

If you have further questions, please do not hesitate to write again.

Very truly yours,

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