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December 16, 1993

Ms. C--- D---
N--- M---, Inc.
XXX --- Avenue
--- ---, Ca XXXXX

Re: SR -- XX-XXXXXX

Dear Ms. D---:

This is in response to your letter dated September 7, 1993, regarding the application of sales and use taxes to sales of tooling to customers from other countries. By letter of August 5, 1993, we outlined the law generally. You have now provided us with copies of actual documents to review, and have requested our opinion as to these documents.

We were provided with two documents. The first is a two page proposal of yours concerning the S--- - G--- project, Israel, dated August 29, 1992.

The second document is a three page Purchase Order of S---, #DSX-SXXX, dated October 22, 1992. A printed portion states "See reverse side for terms and conditions or [sic] purchase." We were not provided with the back portion which may contain terms that would be helpful in this analysis. There is a handwritten notation on page one, near where the lump-sum price for the tooling is circled, that says "Shipped 3/2/93". This makes it appear that the tooling was shipped to Israel before any but the first article was manufactured, but we have nothing that verifies if or how shipping took place. In addition, a typed portion on page three reads:

"After full payment the molds & tools for the above mentioned items will become the property of S--- and held by N--- on behalf of S---. S--- reserves the right to take possession of these items at any time."

To be exempt as a sale in foreign commerce,

"the property must be intended for a destination in a foreign country, it must be irrevocably committed to the exportation process at the time of sale, and must actually be delivered to the foreign country prior to any use of the property."
(Reg. 1620(a)(3)(C)2.)

If payment is made in full, but the tooling is held by you on behalf of your customer, without a contractual duty to deliver or ship it to a foreign destination, the sale of the tooling is fully taxable as a sale which takes place in California. The same would be true even if you did have a contractual duty to deliver or ship the property to a foreign destination, if a functional use is made of the tooling by you, such as manufacturing a run of product, before it is delivered or shipped to the foreign destination.

It appears that the intent of the contract is to have you keep the tooling until some undetermined time in the future. Even then, there is nothing in these documents which require that the property be ultimately delivered or shipped to a foreign destination. Your prior letter indicated that the tooling will always remain in California. If so, sales tax applies to the entire gross receipts from the sale of the tooling. (Annot. 325.0960, 8/6/53.) The only sale that may be eligible for the foreign commerce (export) exemption would be the sale of the manufactured products, provided they are exported under the above cited requirements. (See Reg. 1620, copy enclosed.)

If your contract provides for export of the tooling, and the export meets the requirements of Regulation 1620, including no functional use of the property in this state, the export exemption will apply. Your making of only the test article or articles with the tooling will not be treated as a functional use, and will not in and of itself disqualify the sale of the tooling from the export exemption.

We are still not able to provide you with a positive opinion on your fact situation, because we do not have all the facts. We are not certain of the sequence of events, whether there has been or will be a functional use of the tooling in California, whether there is a contractual duty to export the tooling, or when or if the tooling has or will be actually exported.

If you have other questions, please contact me.

Sincerely yours,

Donald L. Fillman
Tax Counsel

DLF:wk

Enclosure: Reg. 1620