

**STATE BOARD OF EQUALIZATION**

1020 N STREET, SACRAMENTO, CALIFORNIA
(P.O. BOX 942879, SACRAMENTO, CALIFORNIA 94279-0001)
(916) 445-5550

April 23, 1992

Re: ---, Inc.

Dear ---:

This is in response to your letter dated March 5, 1992. You ask whether sales tax applies to your customization of motorcycles in California.

You purchase A motorcycles from locations throughout the United States and thereafter customize them. You state that your production manager, XXX in La Quinta, California, is not your employee but rather is an independent contractor. After the customization is complete, you arrange to have a freight forwarder pick up the motorcycle in La Quinta and export it to a foreign buyer in Japan or Europe. You recently purchased a motorcycle from a dealer in California and the dealer insisted that you pay sales tax (reimbursement), which you did. You ask several questions related to whether sales tax applies to such sales to you in California.

A retailer owes sales tax on the retailer's retail sale of tangible personal property in California. (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.) The sales tax on a retail sale in California is applicable even if, after taking possession of the purchased property in California and prior to any functional use of it, the purchaser ships it outside California. (See generally Reg. 1620.) Thus, when you purchase a motorcycle in California from a California motorcycle dealer, the dealer's sale to you is subject to sales tax unless you are purchasing the motorcycle for resale in the regular course of your business. (Rev. & Tax. Code § 6051.) The tax on such a sale would be a sales tax on the motorcycle dealer. The amount itemized by the dealer to you as "sales tax" would actually be sales tax reimbursement, which the dealer may collect from you by contract. (See Civ. Code § 1656.1.)

On the other hand, if you will resell the motorcycle prior to any use of it, the dealer's sale to you is a sale for resale and would not be subject to sales tax. (Rev. & Tax. Code §§ 6007, 6051.) We agree that the customization process is not a taxable use of the motorcycle if that motorcycle will be resold prior to any functional use. Under such circumstances, you may offer to issue a resale certificate to the vendor in order to avoid paying sales tax reimbursement when purchasing the motorcycle; however, the vendor is not required to accept it. (See Reg. 1668, a copy of which is enclosed.)

You state that you were advised that you could complete a resale certificate as shown in Regulation 1668, and that instead of including a seller's permit number you could substitute "for resale" with your correct corporate name. You understand that since you are an Oklahoma corporation, this would suffice. This is incorrect. The phrase "for resale" is not a substitute for a valid California seller's permit number. Rather, the phrase "for resale" is one of the required elements that any valid resale certificate must contain. Further, that you are an

Oklahoma corporation is irrelevant under these circumstances for purposes of application of the California Sales and Use Tax Law. For example, you could remain an Oklahoma corporation and open a motorcycle shop in California, making sales to California residents from that shop. Notwithstanding that you are an Oklahoma corporation, under such circumstances you would be required to hold a California seller's permit. Similarly, a California corporation who only makes sales in interstate and foreign commerce to non-California residents is not required to hold a California seller's permit, even though it is domiciled and incorporated in California. (Reg. 1699.)

Applying these rules, we agree that you would not be required to hold a California seller's permit if none of your sales were made in this state except sales made in interstate or foreign commerce to non-California residents which qualify for exemption as explained in Regulation 1620. Under such circumstances, and as specifically explained in Regulation 1668, you may issue valid California resale certificates; however, in the location for seller's permit number you must insert an appropriate notation that you are not required to hold a California seller's permit for that reason. (Reg. 1668(b)(2).) Please note that if you make any sales in California which are not exempt from sales tax as sales in interstate or foreign commerce, or if you make any sales of motorcycles for use in California, then you would be required to hold a California seller's permit. Under such circumstances, a resale certificate omitting your valid California seller's permit number would not be valid.

As noted above, the person who owes the sales tax is the retailer. For purposes of the proper administration of the tax, all of that retailer's gross receipts are presumed to be subject to sales tax until the contrary is established. A seller has the burden of proving that a sale of tangible personal property is not a sale at retail unless that seller accepts from the purchaser in good faith a timely and valid resale certificate. (Rev. & Tax. Code § 6091, Reg. 1668.) In the transaction about which you inquire, the motorcycle dealer is the person liable for the sales tax, if any, on the sale of the motorcycle to you. It is possible that the dealer refused to accept the resale certificate that you offered since it was clearly incomplete (it lacked a seller's permit number or an explanation for the reason you are not required to hold a California seller's permit). Another reason might have been that the dealer refuses to accept a resale certificate that does not contain a California seller's permit number since that dealer is the person who must establish that the certificate is valid. There is nothing in California's Sales and Use Tax Law which requires the seller to accept a resale certificate if the seller chooses not to.

Usually, a person purchasing property for resale under circumstances where the seller refuses to accept a resale certificate does not face the same problem as you do. The reason for this is that a retailer reporting California sales and use tax may take a deduction from his or her sales and use tax liability for "tax-paid purchases resold." This is explained in Regulation 1701, a copy of which is enclosed. An example of this procedure is as follows. A person purchases property for \$100 and pays sales tax reimbursement to her vendor. She thereafter resells the property at retail for \$125, and collects sales tax reimbursement on that \$125 from her purchaser. She then reports the sales tax on that sale measured by \$125. From that measure of sales tax she deducts \$100 for the amount of the sales price of merchandise for which she paid sales tax reimbursement and thereafter sold prior to any use. That is, although she pays tax on the full \$125 sale price of the property she sold at retail, her net liability is the tax on the difference of \$25.

Unfortunately, the tax-paid purchases resold deduction is not applicable to your business. In order to take the deduction, the retailer must report to this Board California sales tax from which the deduction is taken. If the retailer has no sales tax liability to this state, then there is no deduction allowed. That is, this is a deduction and not a credit. The retailer may not file a claim for refund for the amount of these taxes unless the retailer

actually reported sales tax to this Board in an amount at least equal to the amount of the claim for refund (the reason for the claim would be that the retailer simply failed to take the deduction in the quarter in which it should have been taken).

In summary, we agree that customization is not a taxable use under circumstances where you will resell the motorcycle prior to any functional use. You may issue resale certificates in order to avoid paying sales tax reimbursement to your vendors, however the vendors are not required to accept them and may choose to treat the sale to you as a retail sale. If the retailer refuses to accept a resale certificate, you will be unable to avail yourself of the tax-paid purchases resold deduction since you report no sales tax to California. Under such circumstances, the choices within your control are to decide whether to purchase the motorcycles from some other vendor or to incur the added cost of the sales tax reimbursement charged by dealers refusing to accept resale certificates from you.

There is one final possibility, but it requires the cooperation of your vendor. Using the following procedure, your vendor can protect itself against owing sales tax without receiving reimbursement from you for that tax liability and still return the reimbursement from you. The first part of this procedure involves doing just what your vendor did: treat the sale as a retail sale, collect sales tax reimbursement from you, and pay the sales tax to California. Upon doing so, the vendor has paid the potential sales tax that the vendor might owe on the sale. The vendor can thereafter file a claim for refund of that tax.

As noted above, when your vendor fails (or refuses) to take a valid resale certificate in good faith, sales tax applies unless the vendor proves the sale was for resale. Assuming the transaction is as described above, with the necessary documentation (from you) your vendor should be able to establish that the sale was for resale. Upon proving that such is the case, the tax would be refunded to your vendor conditioned on your vendor's refunding the sales tax reimbursement to you that your vendor had collected from you. We suggest that you ask your vendor to file a claim for refund of the tax you reimbursed him for to our Refunds Unit at the address above. The claim should specify the amount of the claim, the relevant dates, and the basis for the claim (i.e., the sale was for resale). We suggest also that your vendor include a copy of this letter with the claim. If you have further questions, feel free to write again.

Sincerely,

David H. Levine
Senior Tax Counsel

DHL:cl:4026E

Enclosures

bc: Out-of-State District Administrator