STATE OF CALIFORNIA

BOARD OF EQUALIZATION

395.0490

APPEALS DIVISION

In the Matter of the Petition for Redetermination Under the Sales and Use Tax Law of:	)	SUPPLEMENTAL DECISION AND RECOMMENDATION
C--- W---	)	No. SN -- XX XXXXXX-010
Petitioner	)	

The original Decision and Recommendation dated January 30, 1990, is incorporated herein by this reference. Petitioner has filed a timely request for reconsideration dated April 27, 1990, supplemented by letters dated June 15, and July 3, 1990. The staff has responded by letters dated July 24 and September 4, 1990. James E. Mahler, Hearing Officer.

Petitioner's Contention

The sale of E--- was a nontaxable occasional sale by a partnership.

Summary

The horse E--- was owned by an association of petitioner, Ms. M--- B--- and Ms. N--- C---. The association sold the horse on July 13, 19XX, for $1,500,000. The issue is whether this sale qualifies as an exempt occasional sale.

In previous correspondence with the audit staff and the Hearing Officer, petitioner stated that six horses which had been raced by the association were sold from 1983 through 1988. Four of these horses (including E---) were sold privately, one was sold by auction and one was sold through a claiming race. Petitioner did not explicitly state whether any other horses had been sold prior to being raced. However, in a letter to the audit staff dated July 29, 1987, petitioner had alleged "the uncontroverted fact that prudent horse breeding and racing activities necessarily involve the 'culling' and sale of those animals or interests in animals unfit for racing." Based in part on this allegation, I assumed that other horses had been sold without being raced.

Petitioner now informs me that this assumption was incorrect, and that only the six horses previously named were sold from 1983 through 1988. Another horse was sold at auction in 1981, and one was sold through a claiming race in 1989, for a total of eight sales from 1979 through 1989. All eight horses had been raced by the association prior to sale. Thus, according to petitioner, the following is a complete list of all horses sold by the association from 1979 through 1989:

Year	Horse	Type of Sale	Price
1981	L--- H---	Auction	$ 70,·000
1983	E---	Private	1,500,000
1985	D---	Private	30,000
1986	B--- B--- B---	Auction	35,000
1986	D--- D---	Claimed	50,000
1988	F---	Private	300,000
1988	B--- t--- B---	Private	225,000
1989	P--- C---	Claimed	70,000
			$2;280,000

Petitioner, Ms. B--- and Ms. C--- also previously filed a declaration stating that their association was formed in 1979 with an initial stock of three mares and "the foals produced by such mares, including 'E---' ...." Petitioner now states that the initial stock consisted only of three mares and E---, with no other foals. According to petitioner, the initial stock of four horses was increased by 21 foals over the years, and decreased by eight sales, one death and one horse given away, leaving a stock of 15 horses at the end of 1989. (Petitioner actually claims that 22 horses were "produced" by the association, and that the ending inventory was 17 horses, but the extra horses are not named on petitioner's lists.)

The staff notes that, in addition to the horses owned and sold by the association, petitioner also sold many other horses or fractional interests in horses during the audit period. Since he failed to keep accurate records of his selling activities, however, the staff has been unable to verify whether the above list of sales by the association is complete.

Petitioner also states that the association earned "over $2,000,000" in racing purses from 1979 through 1987, and apparently additional purses in unspecified amounts during 1988 and 1989. Petitioner does not reveal the costs, expenses or losses incurred by the association over those years. He also does not reveal the amounts of any deductions or losses which he may have claimed for income tax purposes with respect to the association's activities.

* * *

An association of individuals may qualify as a partnership for tax purposes only if it is formed to engage in a "business" with the intent to earn a profit. Associations formed to engage in recreational activities or hobbies, without the requisite profit motive, are not engaged in business and thus do not qualify as partnerships for tax purposes. (See the discussion in the original Decision and Recommendation.)

Petitioner has maintained throughout these proceedings that his association with Ms. B--- and Ms. C--- was a partnership formed to earn a profit by breeding and racing horses, with no intent to engage in the business of selling horses. In the original Decision and Recommendation, I concluded that the association had the requisite profit motive and did qualify as a partnership, but my conclusion was not based entirely on the alleged intent to profit from racing. I also found that the association intended to profit from sales of horses. For the same reason, I concluded that the association was in the business of selling horses and was required to hold a seller's permit. Petitioner requests reconsideration in light of the new allegations regarding the association's selling activities.

Analysis and Conclusions

Insofar as is relevant to this case, Revenue and Taxation Code Section 6006.5 defines "occasional sale" to exclude sales of tangible personal property held or used in activities which require a seller's permit Section 6066 of the Code requires every California "seller" to hold a seller's permit. Section 6014 provides that "seller" includes every person "engaged in the business of selling" taxable property. Subdivision (a) (1) of Sales and Use Tax Regulation 1595 further provides: "Generally, a person who makes three or more sales for substantial amounts in a period of 12 months is required to hold a seller's permit ...."

Petitioner relies on the "three or more sales" rule in Regulation 1595. According to petitioner, the association made only eight sales of horses from its inception in 1979 through the end of 1989. Furthermore, petitioner alleges that four of those sales were at auction or through claiming races, and the Board's staff has previously decided that such sales are not to be considered in determining whether a seller's permit is required. (See Sales and Use Tax Annotations 395.0480 [6/10/53] and 395.0520 [2/1/51].) Thus, petitioner admits to only four "countable" sales during an 11-year period and concludes that this level of sales is not sufficient to require the holding of a seller's permit.

I would agree with petitioner's analysis if the "three or more sales" rule were the exclusive test for determining whether a seller's permit is required. It is not the exclusive test, however. Revenue and Taxation Code Section 6066 requires every person engaged in a selling business in California to have a seller's permit, without regard to the number of sales. A person who makes three or more sales may reasonably be presumed to be engaged in a selling business but it does not logically follow that a person who makes fewer sales is not in a selling business. For example, a person in the business of manufacturing and selling boats is clearly engaged in a selling business, no matter how many or how few boats he is able to produce per year.

In his July 29, 1987 letter to the audit staff, petitioner admitted that prudent horse breeding and racing activities necessarily involve the sale of horses found unfit for racing. I agree entirely with this admission. In my view, selling horses is an ordinary and necessary part of breeding horses for racing purposes, even assuming that no horses are ever bred specifically for purposes of sale.

In this particular case, the selling prices in the eight admitted sales total $2,280,000, and of that amount, $2,055,000 was derived from the four "countable" sales. This equals or exceeds the income which the association allegedly received from racing purses. Under these circumstances, it borders on the frivolous to argue that selling horses was an unanticipated or inconsequential part of the association's activities.

For these reasons, I again conclude that the association was engaged in the business of selling horses. This activity required a seller's permit and the sale of E--- therefore does not qualify as an exempt occasional sale.

Because the association was engaged in the business of selling horses, I also continue to believe that the association had the requisite profit motive to qualify as a partnership for tax purposes. If I believed that selling horses was an unanticipated or inconsequential part of the association's activities, however, I would find the evidence insufficient to show that the association was a partnership. In that event, the sale of petitioner's fractional interest in Exploded would be a taxable sale by petitioner individually.

Recommendation

Reaudit as recommended in the original Decision and Recommendation.

_____ 12/20/90

James E. Mahler, Hearing Officer Date