

**STATE BOARD OF EQUALIZATION**

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October 29, 1990

Mr. T--- W. R---
Tax Manager
A--- M--- D---
XXX --- Place
P. O. Box XXXX
---, CA XXXXX-XXXX

SR – XX-XXXXXX

Dear Mr. R---:

This is in response to your letter of October 15, 1990. You have requested an opinion from this office, in accordance with California Revenue and Taxation Code section 6596.

We understand that A--- M--- D--- is a California corporation holding a seller's permit issued in accordance with Revenue and Taxation Code section 6066. Taxpayer is party to several written agreements for the purchase of equipment to be used by taxpayer in this state. Sales tax has been paid with respect to each piece of equipment, and taxpayer has paid sales tax reimbursement to its vendors. Taxpayer intends, prior to the equipment's first functional use, to resell the equipment to a California corporation (the "Leasing Company"). The Leasing Company holds a seller's permit. The Leasing Company will lease the equipment back to taxpayer.

The equipment is state-of-the-art and is customized to taxpayer's specifications by the manufacturers. The equipment has been uncrated and installed by the equipment vendors and is currently undergoing characterization and final acceptance testing. Characterization is the process of defining each machine's processing capabilities. This shakedown/testing process is necessary to assure proper installation and operability to taxpayer's specifications. The equipment cannot be used for production manufacturing until characterization and acceptance are complete.

Taxpayer plans to sell the equipment to Leasing Company, reporting tax on the transaction and collecting sales tax reimbursement from the purchaser. Since no functional use of the equipment has yet occurred, taxpayer plans to claim a tax-paid purchases resold deduction on the return filed for the period in which the equipment is resold to the Leasing Company. Because

the equipment will be resold at taxpayer's cost, the deduction will offset the taxable sale to the Leasing Company.

We are in agreement with your analysis that it is proper for taxpayer to take a tax-paid purchases resold deduction in this case, pursuant to Revenue and Taxation Code section 6012(a)(1), and our Regulation 1701, "Tax-paid Purchases Resold." Specifically, Regulation 1701 authorizes use of this procedure when "the retailer when making the purchase intends to use the property rather than resell it, but rather resells it before making any use thereof." Regulation 1701(b)(1). Field Audit Manual section 0419.25(a) does not apply to this transaction.

Very truly yours,

Gary J. Jugum
Assistant Chief Counsel

GJJ:sr