

**STATE BOARD OF EQUALIZATION**

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December 14, 1995

Account Number

Re: Unidentified Taxpayer

Dear Taxpayer,

This is in response to your letter requesting a ruling with respect to the potential tax liabilities of your client. Initially, I note that the only basis for relief of tax otherwise owed by a person is under specified circumstances when that person reasonably relies on written advice in response to a written request for advice which discloses all relevant facts, including the identity of the taxpayer. (Rev. & Tax. Code § 6596.) Since you have not identified your client, this letter does not come within the provisions of section 6596.

You characterize your client as a broker of logs and lumber who usually does not take title to the logs and lumber it sells, but who occasionally maintains a small inventory outside the state of California. You state that your client's office and storage facility are located outside California, and that it does not have an office or any personnel within this state. It receives orders from customers in California and elsewhere via phone and telex. It does not maintain any trucks or transportation equipment. Instead, it hires independent third party carriers to transport the goods. Title to the goods sometimes transfers to the purchaser at the supplier's location, and sometimes upon delivery to the customer. You present five situations with respect to which you inquire whether your client is required to pay or to collect and remit the tax:

"1. The taxpayer purchases lumber from a California supplier and ships the product to a buyer within the state of California.

"2. The taxpayer purchases lumber from a supplier located outside the state of California, arranges to have the product shipped into California for minor improvements (e.g. having a third party pressure treat lumber), and then arranges to have the improved product shipped to the customer located within California. Occasionally, the product may be in the state of California for more than 30 days while at the third party treater, before being shipped to the customer.

"3. The taxpayer purchases logs and lumber from surrounding states and has the product shipped directly to customers located within California.

"4. The taxpayer may hold product in the State of California which has been sold but cannot be accepted by the buyer immediately. The product may be held 30 days or longer.

"5. The taxpayer purchases product within the state of California and then ships it to a customer located outside of California."

In each of these situations, you indicate that your client purchases the lumber. Therefore, for purposes of this opinion, we assume your questions relate to situations where your client is actually purchasing the lumber and then reselling it, and not situations where your client acts as a true broker. If you have questions regarding brokerage transactions, please write again, and include a statement of the facts you believe support the conclusion that your client acts as a broker, and does not buy and sell lumber on its own account.

A retailer generally owes California sales tax on its retail sales of tangible personal property in this state, unless the sale is specifically exempt by statute. (Rev. & Tax. Code § 6051.) Sales tax does not apply when the sale occurs outside this state. However, when sales tax does not apply, use tax applies to the use of property purchased from a retailer for use in this state, unless the use is specifically exempt by statute. (Rev. & Tax. Code § 6201.) The purchaser owes the use tax. (Rev. & Tax. Code § 6202.) If the retailer is engaged in business in this state, the retailer must collect the applicable use tax from its purchaser and remit that tax to the Board. (Rev. & Tax. Code §§ 6203, 6204.) The purchaser remains liable for the tax until it is remitted to the state unless the purchaser takes a receipt, showing that the tax was paid, from a retailer who is engaged in business in this state or who is registered to collect the use tax. (Rev. & Tax. Code § 6202.)

Except with respect to your fifth situation, there does not appear to be any applicable exemptions. Thus, sales or use tax will be due with respect to the transactions covered by your first four situations. The transaction discussed in your fifth situation may qualify for exemption under Revenue and Taxation Code section 6396, which exempts from sales tax the sale of property that is delivered outside California pursuant to the contract of sale without the purchaser or its agents or representatives having taken possession or control of such property in this state. (Reg. 1620.)

There are three obvious possibilities as to who is responsible for reporting the applicable tax: your client, its customers, or a third party. When the applicable tax is use tax, the purchaser always owes that tax, and must remit it to the state if the retailer does not collect it from the purchaser (e.g., when the retailer is not engaged in business in this state and is not registered to collect the tax and no one else is reclassified as the retailer, the purchaser is required to self-report the tax to the state). However, if your client is engaged in business in this state, it is required to collect the applicable use tax from its customers and remit the tax to this state. On the other hand, if your client is not engaged in business in this state under section 6203 and does not voluntarily register to collect the use tax, the suppliers and third-party treaters discussed in your situations may be reclassified to be the retailers of the lumber. I will discuss this possibility first.

If your client is not regarded as a retailer engaged in business in this state under section 6203, then the second paragraph of Revenue and Taxation Code section 6007, which reclassifies certain persons to be retailers of property when they would not otherwise be so regarded, becomes relevant:

"When tangible personal property is delivered by an owner or former owner thereof, or by a factor or agent of that owner, former owner or factor to a consumer or to a person for redelivery to a consumer, pursuant to a retail sale made by a retailer not engaged in business in this state, the person making the delivery shall be deemed the retailer of that property. He or she shall include the retail selling price of the property in his or her gross receipts or sales price."

Under this provision, any person who is a retailer engaged in business in this state who delivers property to California consumers on behalf of a retailer not engaged in business in this state is regarded as the retailer for purposes of California sales and use tax. (This rule would not apply to a mere common carrier who delivers the property in the course of its common carriage business.) This rule most commonly applies when a wholesaler drop ships property to an out-of-state retailer's California customer. Under the general rules of the Sales and Use Tax Law, the drop shipper would be regarded as making a nontaxable sale to the out-of-state retailer for resale to the California consumer. However, if the out-of-state retailer is not engaged in business in this state, then the drop shipper would be reclassified as the retailer of the property and would be required to report tax on the retail selling price, that is, the amount the consumer pays the out-of-state retailer.¹

If your client is not regarded as a retailer engaged in business in this state, then under section 6007 the person who delivers the property to your client's purchaser may be regarded as the retailer for purposes of paying sales tax and collecting use tax. It appears that this would be the case with respect to the California supplier in situation 1, the third party performing the improvements in situation 2, and any suppliers in situation 3 who themselves are retailers engaged in business in this state. It also appears that in situation 4 there may be a person who would be reclassified as the retailer under the second paragraph of section 6007; however, you have not provided us sufficient information to make that determination. In each case, if under the second paragraph of section 6007 someone other than your client is regarded as the retailer, that person will owe sales tax (when the delivery is from California) or must collect the applicable use tax (when the delivery is from outside California), and that tax will be measured by the amount the consumer pays your client, not the amount you pay the supplier or third party treader.

If, however, your client is a retailer engaged in business in this state within the meaning of Revenue and Taxation Code section 6203, then the second paragraph of section 6007 does not apply. Instead, your client would be required to collect the applicable use tax and remit it to this state. Section 6203 includes several definitions of persons who are "retailers engaged in business in this state." Based on the facts stated in your letter, it appears that the relevant definitions are as follows:

¹ Generally, the applicable tax would be sales tax if the sale occurred in this state (e.g., delivered from California inventory). If the sales tax did not apply, the applicable tax would be use tax.

"(a) Any retailer maintaining, occupying, or using, permanently or temporarily, directly or indirectly, or through a subsidiary, or agent, by whatever name called, an office, place of distribution, sales or sample room or place, warehouse or storage place, or other place of business.

"(b) Any retailer having any representative, agent, salesperson, canvasser, independent contractor, or solicitor operating in this state under the authority of the retailer or its subsidiary for the purpose of selling, delivering, installing, assembling, or the taking of orders for any tangible personal property."

A retailer engaged in business in this state under section 6203 is required to collect the applicable use tax with respect to all its sales to California consumers, not just with respect to those transactions which give rise to the retailer's presence in this state. Thus, if your client is regarded as engaged in business in this state under any of the situations set forth in your letter, or for any other reason, it must collect use tax, when due, with respect to all its sales to California consumers.

It is not clear from your letter whether your client would be regarded as having a place of business in this state. Under some circumstances, a person is regarded as having a business location in this state if its agents or representatives effectively operate a business location in this state on the retailer's behalf. In situation 2, you state that the lumber may be in California for more than 30 days prior to its delivery to the purchaser. If this is solely by virtue of the improvement being performed by the third party treater, it would not generally affect the analysis. However, if the delay in delivery of your client's lumber to your client's customers is at the request of your client, it might raise the question of whether the supplier is operating a business location on your client's behalf. In situation 4, it appears that the location where your client holds property in California may constitute a business location of your client. If so, your client is engaged in business in this state and must pay the applicable sales tax (when the sale occurs in this state and your client's business location in this state is involved in the sale or delivery) and must collect the applicable use tax from its purchasers and pay it to this state.

With respect to subdivision (b) of section 6203, please note that a retailer is engaged in business in this state under this provision if that retailer has any representative or agent in this state for an activity related to sales of tangible personal property. This rule is consistent with the decision in *Quill Corp. v. North Dakota* (1992) 504 U.S. 298, in which the Supreme Court held that a retailer must have some physical presence in the taxing state in order for that state to impose a use tax collection duty on the retailer. In a case in which the retailer's only physical presence in a state was through the use of jobbers, rather than employees, to sell tangible personal property, the Supreme Court held that it was without constitutional significance that the retailer's salespeople were not employees of that retailer. (*Scripta, Inc. v. Carson* (1960) 362 U.S.207.) In *Tyler Pipe Industries, Inc. v. Washington Department of Revenue* (1987) 483 U.S. 232, the Supreme Court held that the showing of a retailer's physical presence in a state cannot be defeated by the argument that the representative was properly characterized as an independent contractor. Therefore, it is not necessary for an individual to be your client's employee, or to act exclusively on your client's behalf, in order for that individual to operate as your client's

representative within the meaning of section 6203(b). (See Business Taxes Law Guide Annotations 220.0100 (11/30/64), 220.0230 (4/10/70).)

We again do not have sufficient information to ascertain whether your client would be regarded as engaged in business in this state under subdivision (b). It appears, however, that it may be regarded as having agents in this state related to sales and delivery of tangible personal property. In this regard, Business Taxes Law Guide Annotation 495.0790 is relevant:

"Agent for Nonregistered Seller. Until an out-of-state retailer with a representative/agent in California registers with the Board as a retailer engaged in business in this state, it may be assumed that the retailer is not engaged in business in this state for purposes of Section 6007. Therefore, all deliveries in this state made by the representative/agent will be assumed to be taxable retail sales by the representative/agent. The representative/agent has the burden of overcoming the assumption by establishing to the satisfaction of the Board that the out-of-state retailer was engaged in business in this state within Section 6203. If the representative/agent satisfactorily overcomes the assumption, the deliveries by the representative/agent will not be considered taxable retail sales even though the out-of-state retailer has not registered with the Board as a retailer engaged in business in this state.

"To overcome the assumption, the representative/agent must establish to the satisfaction of the Board that the out-of-state retailer regularly sells to California consumers and has the tangible personal property delivered by in-state representative/agents. An infrequent sale through an in-state representative/agent will not suffice to overcome the assumption that an unregistered out-of-state retailer is not engaged in business in this state.

"If the representative/agent charges a service fee for completing the required paperwork, which fee the customer must pay to receive the tangible personal property, such fee is subject to tax. When the representative/agent must collect the tax, it should add the fee to the invoice price and collect tax on the total amount. When the out-of-state retailer must collect the tax, it should also collect tax on the invoice price plus the fee, even if the fee is paid directly to the representative/agent by the customer. 8/19/80."

Applying this to your situation 2, if the Board were to audit the third party treater and your client were not registered in California, we would presume that the third party was the retailer of the lumber under the second paragraph of section 6007. To overcome this, the third party treater would have to establish that your client was engaged in business in this state, and might do so simply by establishing that it regularly acted as your client's agent or representative for delivery of property to your client's purchasers. The same analysis applies to the person making the delivery from storage in your situation 4. If your client uses one or a combination of persons to regularly act on its behalf for delivery of property to your client's purchasers, your client would be regarded as engaged in business in this state and would be required to collect the applicable use tax.

In summary, if your client is not engaged in business in this state, any person who is a retailer engaged in business in this state who delivers the lumber on your client's behalf would be classified as the retailer and would be required to report the applicable sales or use tax measured by the retail selling price, that is, the amount paid to your client. However, it appears from the facts you have provided that your client would be regarded as having agents or representatives in this state for purposes of selling or delivering the lumber to California purchasers. If so, your client is required to register with this state for the collection of use tax, and collect the applicable use tax from its California purchasers and remit such tax to this Board. Your client can register by contacting our Out of State District Office at 450 N Street, 19th Floor, P. O. Box 188268, Sacramento, California 95818-0268, or call at (916) 322-2010.

If you have further questions, feel free to write again.

Sincerely,

David H. Levine
Supervising Staff Counsel

DHL/cmm

cc: Out of State District Office (OH)