

STATE OF CALIFORNIA
BOARD OF EQUALIZATION
APPEALS DIVISION

295.0362

In the Matter of the Petition)
for Redetermination Under the)
Sales and Use Tax Law)
)
)
)
)
Petitioner)

HEARING
DECISION AND RECOMMENDATION
No. ----

The above-referenced matter came on regularly for hearing before Hearing Officer W. E. Burkett on September 11, 1990 in Chicago, Illinois.

Appearing for Petitioner:

Appearing for the Sales and Use tax Department: Mr Kurt W. Colin
Supervising Tax Auditor

Mr. Walter J. Cochara
Senior Tax Auditor

Protested Item

The protested tax liability for the period October 1, 1984 through March 31, 1987 is measured by:

<u>Item</u>	<u>State, Local and County</u>
Taxable lease receipts not reported.	\$317,480

Contention of Petitioner

The transfer was an intercompany transfer made to reallocate a business loss on leases of tangible personal property.

Summary

The petitioner is a corporation that engaged in the business of leasing tangible personal property. Petitioner is the successor in interest to ---. This company, --- formerly owned 100 percent of the capital and stock of ---. A prior audit has not been conducted of this account.

The Sales and Use Tax Department (Department) has issued a deficiency determination measured by the California-based share of a payment for assets on lease by petitioner to ---.The leased property consisted primarily of experimental robotics.

The theory of the Department's determination is that there was a retail sale of the leased assets measured by the payments received from ---. It reasoned that the property was not held for resale by -- because it never obtained a seller's permit.

The petitioner contends that the transfer was not intended as a sale of tangible personal property, but rather an intercompany entry made to allocate a business loss suffered by the subsidiary corporation in a venture capital arrangement with a private individual and his two corporations. The two corporations were the lessees. The facts alleged to underly this arrangement are set forth in an affidavit executed by --- Senior Vice President of petitioner dated March 8, 1988. A copy of this affidavit marked as Exhibit A is attached hereto and incorporated herein by reference. The basis for accounting for the transaction is set forth in an intercompany statement is sued on April 12, 1985, a copy of this statement marked as Exhibit B is attached hereto and incorporated herein by reference.

Petitioner's representative pointed out that the basis for the transfer was not the acquisition of the underlying leased property per se but rather to recover its underlying investment in accordance with a prior agreement with the subsidiary. It was noted that --- received a small amount of additional payments from the lessee which was estimated at about \$17,000. Petitioner could not state with certainty whether these payments related to the leases. The equipment, which consisted largely of experimental robotics, was abandoned.

Analysis & Conclusions

It is our conclusion that the allegations set forth in the affidavit of Senior Vice President -- are correct. The impetus for the transfer was not a present bargained for exchange for an assignment of the leases and the underlying property. Rather, it was the prior promise to payoff the leases if the lessees defaulted in their obligation. This promise was given in exchange for petitioner's promise to enter into the leases. This is fully supported by the accounting entries set forth on Exhibit B which do not assign any value to the existing obligation of the lessees.

Notwithstanding the above conclusion, it is clear that --- did receive title to the leased property and that the parties regarded it as having some value. This is indicated by the recital on page two of Exhibit B which proves as follows:

"Please note, as this is an intercompany transfer, --- [sic] will not collect any sales tax on the sale of this equipment, nor is it recapturing any investment tax credit ('ITC'). Should --- decide to sell any or all of the equipment leased under said lease to an outside third party, it will be required to collect and remit to the appropriate taxing authority sales tax on any such sale. In addition, --- would have to recapture any unearned ITC."

In view of the fact that the leased equipment was abandoned and in light of our determination that the transfer was made primarily in furtherance of an antecedent contract

obligation by --- and not a payment for property, it is our conclusion that the amount attributable to gross receipts from a sale of the leased property should be reduced from \$317,480 to \$31,748, the estimated salvage value of the property.

Recommendation

It is recommended that taxes be redetermined on a measure of tax of \$31,748.

W. E. Burkett, Hearing Officer

Date

W/Exhibits A & B

Appeals

Affidavit

State of Illinois)
) SS
County of Cook)

--- being first duly sworn deposes and says:

1. He is currently a Vice President of ---, and at all times prior to June, 1987 relevant to the affidavit, was either a Vice President or a Senior Vice President ---
2. In September, 1982, --- an affiliate of --- advised, --- that it had extended a substantial credit line to --- and the corporations owned by --- including---
3. --- further advised --- that --- and --- were desirous of leasing certain equipment. Since --- was then in the business of leasing equipment, ---- requested that as an accommodation to it, --- enter into equipment, --- leases with --- and --- part of the credit line extended by --- to ---.
4. In accordance with said request, --- entered into the following described equipment leases with both --- and --- (the "Leases"):

<u>Lessee</u>	<u>Lease No.</u>	<u>Date</u>	<u>Aggregate Original Equipment Cost</u>
---	8209700501	9/16/82	\$336,326
---	8310300101	10/11/83	152,308

5. Thereafter, on or about December 1984, --- developed financial difficulties and both - - and --- defaulted under the Leases.
6. As the Leases were entered into by --- as an accommodation to --- on the basis of the credit line granted by --- to ---, on or about April 16, 1985, at the request of --- made an intercompany transfer to --- of \$317,481.43 representing the balance of --- investment in the Leases.
7. At about the same time, and in order to enable --- to consolidate all of its claims against --- on the request of --- assigned to --- on a non-recourse basis all of the right, title and interest of --- on the Leases.
8. The document evidencing the assignment to --- was prepared at the direction of and signed by this Affiant. It was forwarded to --- along with all of --- files with respect to the Leases. No copies were retained by ---.

9. Since that time, --- has been reorganized several times and has undergone a substantial change of personnel. Numerous requests have been made by or under the direction of this Affiant to current employees of --- for copies of the assignment document but it has apparently been lost or misplaced by --- along with the other files of --- with respect to the Leases.

Further Affiant Sayeth Not.

Dated as of March 8, 1988.

Subscribed and sworn to before me a Notary Public in and for the County of Cook, State of Illinois, this 8th day of March, 1988.

Kathy Mazza, Notary Public

To:

InterOffice

From:

Subject: Lease Payoffs as of 4/16/85

Date:4/12/85

Per your request, below please find the amounts necessary for --- to transfer all of the --- leases to --- on 4/16/85:

Schedule 01:

Net investments as of 3/31/85	\$59,480.67	
12/1/84 – 3/31/85 rentals	8,160.68	
Tax due on rentals	530.44	
Late charges on rentals @ 11.15% (through 4/16/85)	227.48	
16 days interest on net investment	<u>209.72</u>	
		\$68,608.99

Schedule 02:

Net investments as of 3/31/85	\$73,670.12	
12/1/84 – 3/31/85 rentals	10,638.68	
Tax due on rentals	691.20	
Late charges on rentals @ 11.20% (through 4/16/85)	297.82	
16 days interest on net investment	<u>361.69</u>	
		\$85,659.51

Schedule 04:

Net investments as of 3/31/85	\$49,938.73	
12/1/84 – 3/31/85 rentals	7,161.40	
Tax due on rentals	465.48	
Late charges on rentals @ 10.85% (through 4/16/85)	194.25	
16 days interest on net investment	<u>237.52</u>	
		\$57,997.38

Schedule 05:

Net investments as of 3/31/85	\$21,824.48	
12/1/84 – 3/31/85 rentals	3,129.72	
Tax due on rentals	203.44	
Late charges on rentals @ 10.85% (through 4/16/85)	84.90	
16 days interest on net investment	<u>103.80</u>	
		\$25,346.34

Schedule 01:

Net investments as of 3/31/85	\$293,001.31	
11/1/84 – 3/31/85 rentals	39,748.90	
Tax due on rentals	0.00	
Late charges on rentals @ 11.60% (through 4/16/85)	1,344.11	
16 days interest on net investment	<u>1,489.89</u>	
		\$335,584.21

Schedule 01:

Net investments as of 3/31/85	\$112,567.43	
2/1/85 – 3/31/85 rentals	6,317.74	
Tax due on rentals	410.66	
Late charges on rentals @ 11.95% (through 4/16/85)	126.17	
16 days interest on net investment	<u>589.67</u>	
		\$120,011.67
		\$693,208.10

Upon our receipt of the \$693,208.10 wire transferred to our account at:

--- will assign to --- all of its rights, title and interest under the aforementioned leases.

Please note, as this is an intercompany transfer, --- will not collect any sales tax on the sale of this equipment, nor is it recapturing any investment tax credit ("ITC"). Should --- decide to sell any or all of the equipment leased under said lease to an outside third party, it will be required to collect and remit to the appropriate taxing authority sales tax on any such sale. In addition, --- would have to recapture and unearned ---.