

Memorandum

325.0088

To : Mr. Dennis Fox
Supervisor, Audit Evaluation
and Planning Section (MIC:40)

Date: September 18, 1995

From : John L. Waid
Senior Staff Counsel

Subject: SY -- XX-XXXXXX ("Taxpayer A")
ST -- XX-XXXXXX ("Taxpayer B")
"FOB Destination" Terms

I am responding to your memorandum to Supervising Staff Counsel David H. Levine dated July 18, 1995 asking for clarification of the rules regarding the role of FOB terms in determining where the sale of tangible personal property takes place for the purpose of determining if sales or use tax applies to a particular transaction. You refer to Annotation 557.0210 but state your view that it does not clearly address whether title to property delivered to a carrier outside the state under the terms FOB Destination passes outside the state. We agree. You attached to your memorandum copies of a facsimile transmission, dated June 29, 1995, from Taxpayer A, questioning the conclusion of the Principal Tax Auditor in a letter to the taxpayer, dated June 1, 1995 (also attached), that a sale takes place at the place where the property is received by the purchaser when the agreement calls for FOB Destination; and a memorandum on the issue, dated February 17, 1995, from Mr. Levine to you.

OPINION

Regulation 1620 states the rules for determining whether the appropriate tax is sales or use tax. Subdivision (a)(2)(A) provides as follows:

"Sales tax applies when the order for the property is sent by the purchaser to, or delivery of the property is made by, any local branch, office, outlet or other place of business of the retailer in this state, or agent or representative operating out of or having any connection with, such local branch, office, outlet or other place of business and the sale occurs in this state." (Emphasis added.)

Regulation 1628(b)(3)(D) provides rules for evaluating where the sale takes place as follows:

"Unless explicitly agreed that title is to pass at a prior time, the sale occurs at the time and place at which the retailer completes his performance with reference to the physical delivery of the property, even though a document of title is to be delivered at a different time or place. If the contract requires or authorizes the retailer to send the property to the purchaser but does not require him to deliver it at destination, the retailer completes his performance with respect to the physical delivery of the property at the time and place of shipment, e.g., delivery of the property to a carrier for delivery by the carrier to the purchaser; but if the contract expressly requires delivery at destination, including cases where one of the terms of the contract is F.O.B. place of destination, the retailer completes his performance with respect to the physical delivery on tender to the purchaser there. When delivery of the property is by facilities of the retailer, title passes when the property is delivered to the purchaser at the destination unless there is an explicit written agreement executed prior to the delivery that title is to pass at some other time."

"Sale" means and includes any transfer of title or possession in any manner or by any means whatsoever of tangible personal property for a consideration. (Rev. & Tax. Code § 6006(a)). (Unless otherwise stated, all subsequent citations are to the Revenue and Taxation Code.) Unless otherwise agreed, title passes at the time and place when the seller completes his performance with respect to physical delivery of the property sold. (Cal. U. Comm. Code § 2401(2); Reg. 1628(b)(3)(D).) Subsection 2319 of the Uniform Commercial Code discusses the effect of an "F.O.B." term, in part, as follows:

"(1) Unless otherwise agreed the term F.O.B. (which means 'free on board') at a named place, even though used only in connection with the stated price, is a delivery term under which

* * *

"(b) When the term is F.O.B. place of destination, the seller must at his own expense and risk transport the goods to that place and there tender delivery of them in the manner provided in this division (Section 2503)...."

California Uniform Commercial Code Section 2503 provides that "tender of delivery" is the seller's responsibility. These three statutes, reflected in Regulation 1628(b)(3)(D), provide rules of general application regarding the place of sale of goods for the purpose of determining if state sales tax or state use tax applies.

Under the above authority, when the sales contract requires the goods to be shipped F.O.B. Destination, the seller does not complete its performance with respect to delivery until the goods are received by the purchaser. Thus, when goods are shipped into California from out of state F.O.B. Destination, the sale occurs in this state. If a local place of business of the retailer participated in the sale, the applicable tax is the sales tax. If, however, there was no participation in the sale by a California office of the retailer, the applicable tax is the use tax even though the sale occurs in this state. (Reg. 1620(a)(2)(A).)

We note that the foregoing are general rules which apply in the absence of a specific clause in the sales agreement providing for title passage at a particular place. As a result, the contract may provide for F.O.B. Destination, but if it specifically provides that title passes at the out-of-state shipping point, the sale takes place there. In that case, the only tax that can apply is the use tax.

In another matter, a taxpayer states in a June 9, 1995 letter that it sent the purchase order to the vendor's San Ramon Regional Office and the purchase order stated the goods were to be shipped F.O.B. Destination. The taxpayer also averred that the proper tax to be applied in that case was the sales tax. Since under the above authority the vendor did not complete its performance with respect to delivery until the property was delivered to the purchaser in California and the vendor's local office participated in the sale, we agree. Sales tax is the applicable tax.

When auditing these kinds of cases, the auditor must first examine the agreement itself for the presence of a title clause and then for a shipping term if a title clause is not present. If there is no title clause or shipping term, the seller completes its performance with respect to delivery upon tender of the goods to the common carrier. (Cal. U. Comm. Code § 2401(2)(a).) If the sale takes place out of state, the only tax that can apply is use tax, and the participation of an in-state sales office is irrelevant. If title is specifically passed in California or the goods are shipped F.O.B. Destination (with no specific title-passage clause), then the sale takes place here, and the question of the participation by an in-state sales office needs to be resolved. Please note that if state use tax applies, so does local use tax. Thus, the resolution of this dispute on the state level will have ramifications for local tax allocation.

JLW:sr

cc: Mr. William D. Dunn (MIC:49)