

STATE OF CALIFORNIA

325.0106

BOARD OF EQUALIZATION

BUSINESS TAXES APPEALS REVIEW SECTION

In the Matter of the Petition)	
for Redetermination Under the)	DECISION AND RECOMMENDATION
Sales and Use Tax Law of:)	
)	
G--- F--- B---)	No. SN -- XX XXXXXX-110
)	
<u>Petitioner</u>)	

The Appeals conference in the above-referenced matter was held by Senior Staff Counsel Stephen A. Ryan on May 5, 1994, in Sacramento, California.

Appearing for Petitioner:

Mr. C--- A---
Attorney

Appearing for the
Sales and Use Tax Department:

Mr. Kevin Hanks
Senior Tax Auditor

Protested Item

The protested tax liability for the period April 1, 1986 through December 31, 1992 is measured by:

<u>Item</u>	<u>State, Local and County</u>
Prices paid to purchase fine art	\$4,834,090
adjustment	(550,000)
	<u>\$4,284,090</u>

A 10 percent penalty was imposed for the failure to file tax returns, but the Department has recommended that it be deleted.

Petitioner's Contentions

1. There is no use tax liability on the purchase and use of some paintings because California sales were made well after interstate commerce deliveries by "sellers" who had sufficient nexus with California, so that the sole tax liability is a sales tax on such sellers with a use tax exemption for petitioner.

2. There is no use tax on the purchase and use of some other paintings because the transferors were private owners who were not retailers engaged in a business and who had not made more than two prior sales in any 12-month period. The involvement of art galleries in these sales is of no consequence because such galleries acted on consignment with the transferors, but without the power to transfer title to petitioner.

Summary

The Sales and Use Tax Department ("Department") contacted art galleries in New York and discovered that many paintings had been purchased for use in California, but with no California use tax paid. One use tax deficiency was imposed upon petitioner's husband, and another upon petitioner as a "dual" determination. According to the Department, each painting had been delivered by a carrier from an out-of-state point to petitioner and her husband in California.

For purposes of the Appeals conference, petitioner has highlighted certain purchases on which she now seeks to obtain nontaxable treatment without conceding taxability on the remaining purchases. The argument is that the sales occurred in California, but for different reasons.

(i) Petitioner first contends that the following paintings were delivered to her to decide if she wanted to buy them, and that only sales tax was incurred by the seller on the later California sales when she decided to make each purchase: O--- "P---"; D--- S--- "U--- XXXX"; F--- "U--- XXXX"; F--- "M--- M---"; H--- "L---"; H--- "P---"; G--- "E---"; H--- "G--- S--- L---"; L--- "P---"; and S--- "R--- of P---".

Mr. B--- submitted a statement signed under penalty of perjury representing that these paintings had been delivered to him and petitioner by galleries for her to decide whether she wanted to buy them. He added for support that other paintings had also been received by them, but were returned unpurchased. A recent letter from J--- G--- Gallery, Inc. ("G---"), to Mr. B--- represents: "R--- of P---" had been delivered on approval to him in order to afford him the opportunity to see it in his home before deciding whether to buy it; such painting had been insured while in transit and at his home until title passed at the time the invoice was issued. The A--- E--- Gallery, Inc. ("E---") and J--- W--- Fine Art ("W---"), also recently wrote to petitioner and her husband with similar representations regarding those remaining paintings, except that for "E---" no reference was made to an "on approval" situation.

In Mr. B---'s letter dated March 12, 1993, he wrote that he had been advised by a gallery that the sellers of the last four above-mentioned paintings had sold more than two paintings in "a twelve month period". G--- also wrote a subsequent letter representing that such gallery had held "R--- of P---" on consignment from a private collector without the power to transfer title "without action on the part of the owner". Petitioner and her husband had been issued a "bill of

sale and warranties" document for the sale of "P---" and "G--- S--- L---" by E---, as "seller", which included a warranty that E--- had "title to or the authority to sell the work". Further, E--- wrote in a later letter to Mr. B--- that it had owned "G--- S--- L---", and had possessed "P---" on consignment as agents for the Estate of the artist with the authority to transfer title. Petitioner and her husband received a sales invoice from W--- for the sale of "E---". W--- later wrote to petitioner and her husband representing that it had held such painting on consignment, but did not have the power to transfer title "without action on the part of the owner".

(ii) Petitioner separately contends that a use tax exemption applies due to the applicability of sales tax on the prices paid for the following paintings because the invoices recite that title in the paintings did not transfer until she completed her payment: C--- "C--- with C--- T---"; D--- "L--- D--- II"; N--- "F---"; P--- "M--- and W--- H---"; and R--- "D--- G--- on B---".

Petitioner and her husband received a sales invoice for each of the latter these paintings from a gallery. Each invoice reads that payment is due upon receipt of the invoice, but that title would not pass until payment was received. Payment was made to each gallery by petitioner after each invoice date with the shortest wait of three days and the longest nineteen days. With Mr. B---'s March 12, 1993 letter, he sent a copy of a letter from The P--- Gallery to him which represented as follows: The transferor-owners of "F---" and "D--- G--- on B---" had confirmed to that gallery that each had not sold more than two works from their collections during any 12-month period; and that such gallery had those paintings on consignment without the power to transfer title to Mr. B---, as the purchaser, "until each respective seller had approved the price that you offered". The M--- D--- R--- Gallery wrote to Mr. B--- regarding "M--- and W--- H---", representing both that the owner of that painting was a financial institution which had become the owner as the rare result of acquiring it as collateral on a defaulted loan, and that such gallery could not have sold that painting "without the approval of the seller at the price offered by [Mr. B---]".

Analysis and Conclusions

1. Although the Department has imposed a use tax upon petitioner, she contends that she is exempt on some purchases on the basis that only the transferors, as "sellers", incurred (sales) tax. Absent an exemption or exclusion, sales tax is imposed upon a retailer measured by the gross receipts she derived from California retail sales of such property (Rev. & Tax. C. § 6051). "Sale" is defined to include any transfer of title or possession of tangible personal property for consideration (Rev. & Tax. C. § 6006(a)). The place of sale is the place where the property is physically located at the time the act constituting the sale takes place (Rev. & Tax. C § 6010.5). Correspondingly, a use tax is imposed upon a person who uses in California tangible personal property which was purchased from a retailer for that use (Rev. & Tax. Code §§ 6004, 6201, and 6202). This liability arises at the time of the first California use (ibid.). "Purchase" is defined basically like the definition of "sale".

As petitioner points out, pursuant to the Sales and Use Tax Law, a sale/purchase can result in either the seller being liable for California sales tax or the purchaser being liable for use tax, but not both (Wallace Berrie & Co. v. State Board of Equalization (1985) 40 Cal.3d 60, 66-67). However, the Board must be satisfied that the gross receipts derived from a sale are included in the measure of sales tax in order for the California use of that property by that purchaser to be exempt from use tax (Rev. & Tax. Code § 6401; Burroughs Corp. v. State Board of Equalization (1984) 153 Cal.App.3d 1152, 1159). The taxpayer has the duty to prove an exemption from use tax (H. J. Heinz Co. v. State Board of Equalization (1962) 209 Cal.App.2d 1, 4).

If the sale occurred in California by a transferor who was a seller-retailer who then had nexus with the State of California as a result of his or her California participation in that sale, then sales tax would apply to that sale, rather than a use tax on petitioner's use (see Rev. & Tax. § 6051; and Regulation 1620(a)(1) and (2)). There is a situation, however, in which no California sales tax will be imposed upon the seller as a result of a California sale, but use tax liability would be imposed upon the California use by the purchaser [absent a use tax exemption or exclusion]. When a California sale is made by an out-of-state seller/retailer who has no "nexus" with the State of California, sales tax will not be imposed because the Board is prohibited pursuant to the U.S. Constitution (see Rev. & Tax. C. § 6352; Reg. 1620(a)(1) and (2); and Norton Co. v. Illinois Rev. Dept. 340 U.S. 534 (1951)).

We find it reasonable that title to, and unconditioned possession (as owner) of, at least some of these paintings may have passed to petitioner in California, such as in any "on approval" sale (see Comm. C. §§ 2326 and 2327). But it is our conclusion that no California sales tax would be applied because there was an insufficient "nexus" with this State to allow the Board to impose sales tax on any transferor -- whether as a private owner, a gallery, or other seller-retailer. [As discussed, *infra*, we treat each disputed transaction as having involved a transferor who was of a status capable of sales tax liability.] None of the owners or galleries was at the time of any sale physically present in California in an office or other place of business. The mere presence in California of a painting on the date of sale is not a sufficient basis to establish nexus for that sale. The required nexus also does not arise merely from the prior presence here of other paintings which were delivered and sold in California by the same owner or gallery in this same fashion. Without particular evidence of some type of place of business in California for the purpose of taking the sales order or delivering the property, whether personally by the owner or gallery, or through their agents or representatives, it has not been established that nexus then existed in order for sales tax to have been incurred on any sale (Reg. 1620(a)(2)). The Board has chosen not to extend sales tax beyond the Regulation 1620(a)(2) scenarios. Since there was no office of any owner or gallery in California, no nexus existed and petitioner has thus not proven to the satisfaction of the Board that a use tax exemption is applicable under Revenue and Taxation Code section 6401. The different use tax collection decisions mentioned

by petitioner, including Quill Corp. v. North Dakota, 112 S.Ct.1994 (1992), do not constitute authority on this direct sales tax issue.

It is possible that one or more of these disputed sales occurred outside California. Petitioner has not satisfactorily verified the time or location of each particular sale since we do not possess the actual shipping documents to verify the locations of the paintings during the relevant times, or any "on approval" correspondence which would verify petitioner's alleged right to return paintings in her possession without incurring any charge. On any sale which occurred outside California, no California sales tax could apply since sales tax can only be incurred when the sale occurs in this State (Rev. & Tax. C. § 6051; Reg. 1620(a)(1)).

As to (ii), for any paintings which were already accepted by petitioner, the attempted withholding of title thereafter until such time that payment was made, did not delay the "sale" or legal transfer of title since the retention by the seller of title in goods already delivered to the buyer is limited in effect to a reservation of a security interest (Commercial Code § 2401(1); and Rev. & Tax. C. § 6006(e)). Without verification of the earlier time or the location of those paintings in (ii), petitioner has not proven the application of the section 6401 use tax exemption.

3. One typical manner in which a California person does not incur use tax liability on the purchase and California use of artwork is an occasional sale of such property which had not been held by the transferor in the course of activities for which he/she/it was then required to hold a seller's permit or who would have been required to hold a seller's permit if the activities had been conducted in California; provided that the sale was not one of a series of sales sufficient in number, scope, and character to constitute an activity for which a permit was or would have been required (Rev. & Tax. C. §§ 6367, and 6006.5(a)). The transferor is then also exempted from sales tax liability. Whether the purchase occurs in or outside California is irrelevant. The important point on this subject is that such transferor is not a "seller" or a "retailer".

Petitioner contends that some other owners were not sellers. It is rebuttably presumed that property shipped or brought into California by the purchaser was purchased from a "retailer" (Rev. & Tax. Code § 6246). Further, although petitioner has submitted several letters which purport to label several owners as non-retailers and/or non-sellers who were not engaged in business or otherwise selling any paintings at the time of sale ("F---", "M--- and W--- H---", "D--- G--- on B---", and possibly "R--- of P---"), each sale also involved the actions of a gallery which was both engaged in business transferring title to paintings, and which transferred to petitioner the title in the respective paintings in question.

It appears that at least some galleries acted in a consignment relationship with the owner, while others may have been a sales agent. Each letter from these particular galleries either expressly or impliedly admits that it had the power to transfer title in the respective painting to petitioner. Some of that authority was restricted to a time after the occurrence of conditions, all of which

had actually occurred prior to each sale which was consummated through the actions of the respective gallery to transfer title by delivery of the painting, the invoicing to petitioner, and collection of the purchase price.

The Board has a long history of imposing a sales tax liability or a use tax collection and remittance debt, as appropriate, on consignees and other non-owners who transfer to the purchasers the title in the goods belonging to another person (see Regulation 1569; and Annotations 185.0140 [1-28-66]; and 185.0180 [6-13-50]). It is our conclusion that this involvement of the gallery-seller-retailers as consignees or otherwise, is sufficient to prevent application of the occasional sales exemption as defined in § 6006.5(a) because a “seller” transferred to petitioner the title in each painting.

Recommendation

Redetermine with the only adjustment being to delete the penalty.

Stephen A. Ryan, Senior Staff Counsel

Date