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January 13, 1993

Mr. J--- M---
P---, Inc.
XXX --- Street
--- ---, CA XXXXX

Re: SR – XX-XXXXXX

Dear Mr. M---:

This is in response to your letter dated November 6, 1992. P--- is an advertising specialty company with offices in --- and --- --- Counties. You have set forth four scenarios about which you inquire as to the proper application of sales and use tax. Each is quoted below followed by my response.

"1) XYZ Company has offices worldwide with headquarters in Santa Clara County.

"XYZ Company sends a purchase order to P---, Inc. to purchase merchandise for XYZ Company logo'd merchandise.

"P--- Inc. bills XYZ Company for all merchandise received and held in --- --- warehouse.

"As needed different departments of XYZ Company requests specific quantities to be sent to their various locations worldwide.

"Once a month P--- Inc. bills XYZ Company, Headquarters, for fulfillment and shipping costs associated with the requests.

"The XYZ Company logo'd merchandise is for new employees hired throughout all locations of XYZ Company - worldwide. XYZ Company never takes possession of the merchandise. The merchandise is intended as a gift to new employees of XYZ Company.

"Question: At what stage does the merchandise become taxable and at what rate?"

The initial critical question is when and where P---'s sales to XYZ occur, and your description does not clearly answer this question. The sale of tangible personal property occurs upon transfer of title to that property from the seller to the purchaser. (Rev. & Tax. Code § 6006.) When a contract of sale is silent with respect to transfer of title, title is transferred when the seller completes its responsibilities with respect to physical delivery of the property. (UCC § 2401.) When the property is shipped to the purchaser by common carrier, the seller completes its responsibilities with respect to physical delivery of the property upon tender of the property to the common carrier for shipment to the purchaser.

Although you do not describe the manner of delivery, I assume that the property is delivered to a common carrier in --- ---. Based on this assumption, if the contract of sale did not otherwise provide for passage of title, the sale would occur when P--- delivered the property to the common carrier. However, you state that P--- bills XYZ for all merchandise received and held in [P---'s] --- --- warehouse. I therefore assume that provisions of the contract of sale would be interpreted to pass title to XYZ upon delivery to P---'s --- --- warehouse, and the remainder of this opinion is based on this assumption. (If you disagree, you should write again and include a copy of the contract and all other relevant documents.)

Sale tax applies when the sale occurs unless the sale is specifically exempt by statute. Since the sales about which you inquire occur upon delivery to P---'s warehouse, sales tax applies at that time unless an exemption applies. The exemption relevant to this discussion is the exemption provided by Revenue and Taxation Code section 6396 for sales in interstate commerce. This exemption is explained in Regulation 1621, a copy of which is enclosed. To qualify for the exemption, the contract of sale must require the property to be shipped outside California, and the property must, in fact, be shipped outside California.

Your description of the contract indicates that it does not require the property to be shipped outside California. Rather, it appears that the contract requires P--- to ship the property to whatever location XYZ specifies at the time it instructs P--- to ship the property. It therefore appears that P---'s sales to XYZ are not entitled to the exemption for sales in interstate commerce. This means that all sales by P--- to XYZ would be subject to tax, at the time of the sale (delivery to --- --- warehouse), at a rate of at least 7 1/4 percent, the minimum combined statewide rate.¹

¹I note that my conclusion that none of P---'s sales to XYZ qualify for the exemption from sales tax for sales in interstate commerce is based on assumptions made with respect to the contract between P--- and XYZ. If the contract instead provided that the sale did not occur until shipment by P--- from its warehouse, the sale of property which is shipped outside California might qualify for the exemption. However, without a more complete description of these arrangements and a copy of the relevant documents, including the contract, I am unable to reach such a conclusion.

Any tax which may be applicable above 7 1/4 percent would be a tax adopted by a district pursuant to the Transactions and Use Tax Law. (Rev. & Tax. Code § 7251, et seq.) I will refer to such taxes as "district" taxes. A district's sales tax is applicable to sales occurring in that district unless the sale is otherwise exempt from the district sales tax. The exemption relevant to this discussion is the exemption for a sale of property which is shipped to a point outside the district pursuant to the contract of sale. (Rev. & Tax. Code § 7261(a)(6).)

A district's use tax is applicable to property purchased outside the district for use inside the district. If the sale is subject to one district's sales tax, but the property is purchased for use in a second district, the purchaser is entitled to a credit against the second district's use tax for any district tax paid to the first district or a credit for any reimbursement paid to a retailer for the first district's tax. (Rev. & Tax. Code § 7262(a)(4).)

There is currently a 1/4 percent district tax imposed in --- County. When P--- makes taxable sales of tangible personal property in --- County, the applicable combined sales tax rate is 7 1/2 percent unless the transaction qualifies for the exemption provided by subdivision (a)(6) of Revenue and Taxation Code section 7261. For the same reasons that I have concluded that P---'s sales to XYZ are subject to tax even if the items are thereafter shipped outside California, I must also conclude that P---'s sales to XYZ are subject to the 1/4 percent district sales tax imposed in --- County even if the property is thereafter sent outside --- County.²

If XYZ were to make a gift of property to a person in Los Angeles and P--- were to ship that property on XYZ's behalf from --- --- *directly* to the donee in Los Angeles, the district tax imposed in Los Angeles would not apply. The reason for this is that XYZ would have consumed the property in --- --- when P--- sent it to the donee. That is, a person who transfers property without receiving any consideration is the consumer of that property for purposes of application of sales and use tax. (See, e.g., Business Taxes Law Guide Annotations 165.0040 (4/1/53), 165.0060 (2/7/66, 7/5/89).) We have always regarded that consumption, that is, the use, to have occurred when title passes from the donor to the donee. If a donor transfers property to a common carrier in one district for shipment to a donee in another district, the donor has consumed the property in the district from which it was shipped at the time the donor has made all the use of the property that the donor ever will, that is, at the time the donor gives it away.

However, we do not believe that XYZ transfers title to the property to donees in --- ---. Although you state that XYZ never takes possession of the property, you also state that the property is shipped to XYZ's various locations. Thus, we conclude that XYZ does in fact take

²Similar to my note above, I note that my conclusion that none of P---'s sales to XYZ qualify for the exemption from the 1/4 percent district sales tax imposed in --- County for a sale of property which is shipped to a point outside the district pursuant to the contract of sale is based on assumptions made with respect to the contract between P--- and XYZ. If the contract instead provided that the sale did not occur until shipment by P--- from its warehouse, the sale of property which is shipped outside --- County might qualify for the exemption from the district tax imposed in --- County. However, without a more complete description of these arrangements and a copy of the relevant documents, including the contract, I am unable to reach such a conclusion.

possession of the property at its various locations and that the property is not sent from --- --- directly to donees. It appears likely that the property is distributed to the employees from those various XYZ locations, and XYZ would be regarded as using the property at those locations.

Following is a summary of the specific application of tax to the transactions at issue based on the facts in your letter and the assumptions and analysis set forth above. All P---'s sales to XYZ are subject to the statewide rate of 7 1/4 percent plus the 1/4 percent tax imposed in --- --- for a total minimum tax of 7 1/2 percent. This amount is a sales tax, imposed on P---, for which P--- may collect reimbursement from XYZ if their contract so provides. (Civ. Code § 1656.1.) When P--- ships property into a district which imposes a district tax, XYZ will owe that district's use tax, but will receive a credit for the 1/4 percent --- County district sales tax for which (I assume) P--- collects reimbursement. For example, if P--- ships property to XYZ in Los Angeles, which has district taxes in a total amount of 1 percent, XYZ will owe an additional 3/4 percent use tax. (Whether P--- would be required to collect that additional use tax is discussed in response to your next scenario.)

"2) FOR SALES ORDERS THAT ARE FAXED, PHONED OR MAILED INTO P---
Inc. - --- COUNTY

- "A. Orders that ship to --- County are to be charged 7-1/2% sales tax. (This is because P---, INC. does business in --- County).
- "B. Orders that ship to --- --- County are to be charged 8-1/4% sales tax. (This is because P--- INC. does business in --- --- County).
- "C. All other orders that ship to the other 50 counties in California [I assume that this is a typo and that your inquiry relates to the 56 other counties in California] are to be charged 7-1/4% sales tax.

Initially, I assume this inquiry relates to the general sales transaction: the purchaser places the order and P--- ships the property to the purchaser as required by their contract, with passage of title at the time of shipment. The general rules discussed with respect to your previous scenario are also applicable here. When the property is shipped from the --- --- warehouse to a purchaser in --- County, the district sales tax imposed in --- County applies. Thus, the total sales tax rate is 7 1/2 percent. P--- owes this sales tax, and may collect reimbursement from its purchaser if the contract of sale so provides.

When the property is shipped from --- --- to a purchaser outside --- County pursuant to the contract of sale, the transaction is exempt from the district sales tax imposed in --- County. If the property is shipped to a purchaser outside --- County for use in a county which does not have any district taxes, then the total tax rate is 7 1/4 percent. If, however, the property is purchased for use in a county which has a district tax, that district's use tax applies.

P--- may voluntarily register to collect all district taxes imposed by districts in California. If it were to do so, it would be required to collect the applicable district use taxes for all districts imposing district taxes. (See Reg. 1827.) However, assuming it does not do so, P--- is only required to collect the applicable district use tax with respect to those districts in which it is engaged in business. This is explained in Regulation 1827, a copy of which is enclosed. Assuming that P--- is engaged in business only in --- and --- --- Counties, it would only be required to collect the district use taxes imposed by districts encompassing those counties. (As discussed below in response to your next scenario, it appears that P--- is actually engaged in business in counties other than just --- and --- ---.)

Districts imposing district taxes are generally coterminous with county boundaries. There is currently one district imposing a district tax which extends beyond the boundaries of a single county, the Bay Area Rapid Transit District (BART). BART comprises Contra Costa County, Alameda County, and San Francisco County and imposes a tax of 1/2 percent.³ Since P--- is engaged in business in --- --- County, it is engaged in business in BART. When it ships property from --- --- to a purchaser in --- --- County, P--- is required to collect a total of 1 percent of district use taxes. When P--- ships property to a purchaser in San Francisco or Alameda, it is required to collect the 1/2 percent BART district tax. However, assuming it is not engaged in business in San Francisco or Alameda Counties, P--- is not required to collect the other district use taxes imposed in those counties. The purchasers would, however, be liable for those additional district use taxes.

"3) FOR SALES ORDERS THAT ARE ACTUALLY OBTAINED BY A P--- REPRESENTATIVE IN PERSON- (i.e.- road shows, presentations)

- "A. If an order is obtained by a P--- INC. representative in a given county and is delivered to that same county, then it is that county's sales tax rate that applies.
- "B. If the P--- INC. representative obtains the order in a given county and the order ships to a different county, other than --- or --- ---, then a sales tax rate of 7-1/4% applies."

The analysis set forth above is also applicable to this scenario. Whether P--- is required to collect the applicable district use tax depends on whether it is engaged in business in that district. As explained in subdivision (c) of Regulation 1827, "retailer engaged in business in a district" is defined to include:

³Counties may contain more than a single district imposing a district tax and since the districts may all have the same boundaries, it is often not necessary in this type of opinion to break down the various district taxes. The three counties comprising BART each contain a separate additional district which imposes a district tax, and for this discussion it obviously is necessary to distinguish the tax imposed by BART from the taxes imposed by other districts in San Francisco and Alameda.

"(1) 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 in the district.

"(2) Any retailer having any representative, agent, salesman, canvasser or solicitor operating in the district under the authority of the retailer or its subsidiary for the purpose of selling, delivering, or the taking of orders for any tangible personal property."

Applying these rules to the scenario you present, if a P--- representative solicits an order at a road show or presentation, or in any other way while physically present in a district, then P-- - is a retailer engaged in business in that district. This means the P--- must collect that district's use tax on *any* sales delivered into that district (whether or not the particular sale is one of those solicited in that district in person).

Under your scenario 3(A), P--- would be a retailer engaged in business in the district in which the representative obtained the order and would therefore be required to collect the tax applicable in that district. Under your scenario 3(B), you have provided insufficient information for me to provide you a definitive answer. The fact that the property is delivered to a district other than the district where the order was obtained is not determinative. For example, if the property were delivered to another district in which P---'s representative had solicited orders, P-- - would be regarded as engaged in business in that district and would be required to collect its district use tax.

"4) XYZ Company purchases merchandise from P--- Inc. which is held in our Rohnert Park warehouse.

"P--- Inc. bills XYZ Company for all merchandise received and held at the --- --- warehouse.

"Consumers throughout the U.S., buy the XYZ Company logo'd merchandise, from P--- Inc.

"P--- Inc. reimburses XYZ for the merchandise.

"ie: XYZ buys 250 hats @ \$10.00 each from P--- Inc. The 250 hats are inventoried at P--- Inc. - --- ---. Customer buys one hat @ \$15.00 each from P--- Inc. P--- Inc. reimburses XYZ \$10.00 for the sale."

Without reviewing all relevant documents, I am unable to provide you with a definitive

response because the relevant facts are not entirely clear. For example, you state that consumers purchase the property from P---, but does P--- make the sales on its own behalf or actually make the sales on behalf of XYZ? What happens to hats which are not sold by P---?

One possibility is that XYZ is purchasing the items for resale to P---, who would be purchasing the items for resale to consumers. If such is the case, the sales by P--- to the consumers would be the retail sales subject to tax. The rate of that tax would be 7 1/4 percent plus any tax imposed by the district to which P--- delivers the purchased property. As explained above, P--- would be required to collect that district tax if it is engaged in business in that district. In any event, the purchaser would owe the district tax even if P--- were not required to collect it. Another possibility is that XYZ is selling the property to consumers. If so, XYZ would owe sales tax, or be responsible for collecting use tax, measured by the sale price to the consumers.

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

Sincerely,

David H. Levine
Senior Tax Counsel

DHL:cl

Enclosures

bc: --- --- District Administrator
Local Tax