The protested tax liability for the period July 1, 1988 through June 30, 1991 is measured by:
Item          State, Local and County

A. Claimed exempt sales disallowed, $5,000 and less, by sample $1,571,785
B. Claimed exempt sales disallowed, $5,001 to $24,999, by sample 529,550
C. Claimed exempt sales disallowed, $25,000 and greater, actual 66,289

Total        $2,167,624

Contentions

Petitioner contends that:

1. The sales were exempt sales to a common carrier.
2. The sales were exempt sales in foreign commerce.
3. The sales were exempt sales of property which became part of a watercraft.
4. Relief should be granted because the customer was following written advice from the Board.

Summary

Petitioner is a corporation which is engaged in selling electrical parts for ships and industrial equipment at retail and for resale. The last scheduled audit was for the period through June 30, 1987 and was waived by the Department.

The auditor reviewed petitioner's records for sales claimed to be exempt sales to common carriers. Transactions which the auditor regarded as not adequately supported to qualify for exemption were held by the auditor to be taxable. The deficiencies noted by the auditor included bills of lading showing the buyer, rather than petitioner, as the consignor or shipper, bills of lading which were not signed by the carrier, and missing bills of lading. Petitioner disputes that any sales made to A--- P--- L--- (APL) were taxable.
Petitioner states that it is the practice of APL to combine purchases of property for its own use from several vendors on one bill of lading for its own convenience. It is also the practice of APL to send its vendors a copy of each bill of lading upon which the products sold by that vendor were shipped. Petitioner states that APL's process was approved by the Board by letter dated October 10, 1985 to Mr. D--- Z---, Manager of Tax Research and Planning for APL from Mr. Glenn A. Bystrom, Principal Tax Auditor. A copy of the letter is attached as Exhibit I. A typical bill of lading issued by APL and disallowed by the auditor is attached as Exhibit II. The bill of lading shows APL as well as the vendors as consignors or shippers. Petitioner also contends that where APL furnished copies of bills of lading to petitioner at the time of the audit because petitioner's records did not contain copies of the bills of lading, it should be assumed that originals of the bills of lading were timely issued by APL and received by petitioner. Petitioner further contends that bills of lading should not be disallowed on mere technicalities. The intent of the parties should be considered. Petitioner argues that it should not be held liable for deficiencies in the APL procedure because it has no control over APL and is only a minor supplier. The transactions in question should be regarded as exempt sales to a common carrier. Petitioner cites as support Business Taxes Law Guide (BTLG) Annotation 500.0060 (2/19/53). Petitioner points out that it accepted all exemption documentation from APL in good faith and contends that it should therefore be relieved of liability for the tax.

Petitioner also contends that the sales qualify as exempt sales in foreign commerce. The property was shipped to points outside the United States and was properly regarded as exports. There was a certainty that the property would be exported when it left petitioner's hands. Petitioner cites as support McDonnell Douglas v. State Board of Equalization (1992) 10 Cal.App.4th 1413. Petitioner also cites BTLG Annotations 325.0280 (8/20/51) and 325.1160 (1/17/55).

At the Appeals conference, petitioner raised a new issue. This issue was that the sales qualified as exempt sales of property for use on watercraft which were transporting property for hire in interstate commerce or foreign commerce. Because this argument had not been considered by the auditor, the auditor was allowed time in which to respond to the argument. The audit staff, after a preliminary investigation, stated that there was no evidence that the items purchased by APL became permanent parts of vessels.

Analysis and Conclusions

Common Carrier Exemption

Section 6385 of the Revenue and Taxation Code provides in subdivision (a):

"There are exempted from the computation of the amount of the sales tax the gross receipts from the sale of tangible personal property, other than fuel and petroleum products, to a common carrier, shipped by the seller via the purchasing
carrier's facilities under a bill of lading whether the freight is paid in advance, or the shipment is made freight charges collect, to a point outside this state and the property is actually transported to the out-of-state destination for use by the carrier in the conduct of its business as a common carrier."

The property in question was carried by the purchasing carrier's facilities to a point outside this state for use by the carrier in the conduct of its business as a common carrier. That alone is insufficient to establish the exemption. The statute also requires that the property be shipped by the seller under a bill of lading. Obviously the bill of lading must be in proper form. The statutory requirement is accomplished by showing the seller as the consignor or shipper on the bill of lading. The statute does not merely make sales to common carriers exempt. It makes the sales exempt only if the seller ships the goods under a bill of lading. Thus, the form is the essence of the exemption. See Satco, Inc. v. State Board of Equalization (1983) 144 Cal.App.3d 12. Defects in the documentation are fatal to the exemption.

Sales and Use Tax Regulation 1621 deals with this exemption. Subdivision (c)(1) provides:

"Any seller claiming a transaction as exempt from sales tax under Section 6385(a) must receive at the time of the transaction, and retain, a properly executed bill of lading, or copy thereof, pursuant to which the goods are shipped. The bill of lading must show the seller as consignor. It must indicate that the described goods are consigned to the common carrier at a specified destination outside this state. Where the form of the transaction is `freight collect,' no specific freight charge need be shown on the bill of lading, inasmuch as such charges are not ordinarily shown thereon in `freight collect' transactions. Furthermore, the carrier need not actually collect freight charges from itself. The form and language of the bill of lading should be similar to the form and language normally used where the purchaser and carrier are not the same. A bill of lading will be considered obtained at the time of the transaction if it is received either before the seller bills the purchaser for the property, within the seller's normal billing and payment cycle, or upon delivery of the property to the purchaser.

"In addition to a bill of lading, the seller must obtain from the purchaser prior to or at the time of the transaction, and retain, a certificate in writing that the property shall be transported and used in the manner described in subdivision (b)(1) of this regulation. The certificate shall be in substantially the same form as Certificate A or B, appearing in the appendix of this regulation. Certificate B may be used when multiple transactions claimed as exempt are made between a seller and a carrier and may be included as part of a transaction by reference to the certificate on the purchase order or other appropriate documentation for each transaction."
Where the buyer is shown as the consignor, the bill of lading is not acceptable. Further, a bill of lading serves two purposes. It is a contract for transportation and is also a receipt for the property shipped. If there is no signature, it cannot serve as a receipt and is unacceptable. The regulation requires that the sellers receive the bill of lading timely and retain it. Thus, obtaining a copy of the bill of lading for purposes of the audit to replace a bill of lading that is not in the seller's file is unacceptable. While exemption documentation taken in good faith relieves a seller of liability for sales tax, that documentation must be in proper form. The "taking in good faith" phraseology merely means that the seller must not have knowledge that the buyer does not intend to use the property in an exempt manner, even though properly executed documentation is taken by the seller.

Petitioner states that BTLG Annotation 500.0060 supports its position. That annotation, which is no longer in the BTLG, stated that if bills of lading are made out sufficiently complete so as to meet all of the requirements of laws and regulations covering bills of lading issued by common carriers, copies of such bills in the hands of vendors will be sufficient for purposes of Section 6385 exemption with respect to sales to common carriers. The point is that the bills of lading held by petitioner are not sufficiently complete. Further, the regulation which was issued at a later date than the annotation specifically states requirements for exemption and had precedence over the annotation.

Section 6596 provides:

"(a) If the board finds that a person's failure to make a timely return or payment is due to the person's reasonable reliance on written advice from the board, the person may be relieved of the taxes imposed by Sections 6051 and 6201 and any penalty or interest added thereto.

"(b) For the purpose of this section, a person's failure to make a timely return or payment shall be considered to be due to reasonable reliance on written advice from the board, only if the board finds that all of the following conditions are satisfied:

"(1) The person requested in writing that the board advise him or her whether a particular activity or transaction is subject to tax under this part. The specific facts and circumstances of the activity or transaction shall be fully described in the request.

"(2) The board responded in writing to the person regarding the written request for advice, stating whether or not the described activity or transaction is subject to tax, or stating the conditions under which the activity or transaction is subject to tax.
"(3) In reasonable reliance on the board's written advice, the person did not do either of the following:

"(A) Charge or collect from his or her customers amounts designated as sales tax reimbursement or use tax for the described activity or transaction.

"(B) Pay a use tax on the storage, use, or other consumption in this state of tangible personal property.

"(4) The liability for taxes applied to a particular activity or transaction which occurred before either of the following:

"(A) Before the board rescinded or modified the advice so given, by sending written notice to the person of the rescinded or modified advice.

"(B) Before a change in statutory or constitutional law, a change in the board's regulations, or a final decision of a court, which renders the board's earlier written advice no longer valid.

"(C) Any person seeking relief under this section shall file with the board:

"(1) A copy of the person's written request to the board and a copy of the board's written advice.

"(2) A statement under penalty of perjury setting forth the facts on which the claim for relief is based.

"(3) Any other information which the board may require.

"(d) Only the person making the written request shall be entitled to rely on the board's written advice to that person."

The October 10, 1985 letter which petitioner contends authorized the type of documentation issued by APL was not addressed to petitioner. Thus, under the express terms of the statute, petitioner was not entitled to rely upon it. However, aside from this problem, the letter authorizes the use of multiple consignors or shippers when the listed consignors or shippers are vendors. It does not authorize the listing of APL as one of the consignors or shippers. It does not authorize the use of incomplete bills of lading. In conclusion, the October 10, 1985 letter forms no basis whatsoever for relief.
Petitioner contends that it should not be held liable because APL controls the issuing of the documentation. Section 6091 provides that the burden of showing that a sale is not taxable is on the seller. Petitioner is required to pay tax unless it can demonstrate that the sale is not subject to tax or is exempt. The documentation is a matter between petitioner and its customers and the issuing of improper documentation by the customers does not relieve petitioner of liability.

Foreign Commerce Exemption

Section 6352 exempts from tax sales and uses which the state is prohibited from taxing under the Federal Constitution. The Federal Constitution bars the imposition of tax on sales in foreign commerce. Regulation 1620 provides in subdivision (a)(3)(C) that sales tax applies when the property is delivered in this state to the purchaser prior to an irrevocable commitment of the property to the process of exportation. It is immaterial that the disclosed or undisclosed intention of the purchaser is to ship or deliver the property to a foreign country or that the property is actually transported to a foreign country. Movement of the property into the process of exportation does not begin until the property has been started upon a continuous journey to the foreign destination.

Petitioner cites the McDonnell Douglas case in support of its contention that the sales here were exempt sales in foreign commerce. The facts are distinguishable. In McDonnell Douglas, the goods were shipped to the facility of an export packer. The court regarded such shipment as entering the goods upon a continuous journey to a foreign destination. The Board's position in that case was that, although the property was shipped to an export packer, the buyer's employees actually prepared the property for export at the packer's location. The court apparently found this distinction to be immaterial. In Rice Growers Association of California v. Yolo County (1971) 17 Cal.App.3d 227, cert. den., 404 U.S. 941, the court held that shipment of property to the collection point of the buyer did not constitute the entering of the property into a continuous journey to a foreign destination. I conclude that the Rice Growers case is applicable here. Petitioner's sales of property were not exempt sales in foreign commerce. The annotation cited by petitioner deals with the bill of lading requirements for sales in foreign commerce. These sales were not sales in foreign commerce regardless of the adequacy or inadequacy of the bills of lading.

Watercraft Exemption

Section 6368 in pertinent part exempts from tax sales of tangible personal property which become component parts of watercraft if the watercraft is used in interstate or foreign commerce involving the transportation of property or persons for hire. The auditor, after review of petitioner's contention, agrees that there is a potential application of this exemption. However, there is no evidence to show that the property became component parts of vessels. APL's vessels are admittedly used for the transportation in interstate or foreign commerce of property or
persons for hire. The question is whether the property sold by petitioner to APL became component parts of the vessels. Items listed on invoices include plugs, connectors, housings, regulators, switches, pumps, relays, actuators, carbon brushes, contacts, cables, solenoids, volt meters, capacitors, resistors, and ammeters. It is not possible from these descriptions to determine with certainty whether the items become component parts of the vessels. Section 6091 places the burden of proof on the seller. A party claiming a tax exemption has the burden of showing that he comes within the terms authorizing exemption. See Standard Oil Company of California v. State Board of Equalization (1974) 39 Cal.App.3d 765 and H.J. Heinz Company v. State Board of Equalization (1962) 209 Cal.App.2d 1. Petitioner has presented a valid legal argument but has not submitted any detailed evidence to support the grounds for exemption of any specific item. Petitioner should be allowed sixty days in which to supply appropriate evidence to the auditor. A reaudit should be performed to delete from the amount subject to tax any transactions which qualify for the watercraft exemption.

Recommendation

Allow petitioner sixty days in which to supply evidence that any transactions qualify for the watercraft exemption. Reaudit to delete from the amount subject to tax those transactions for which satisfactory evidence is submitted.