

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION

325.1150

In the Matter of the Petition )  
for Redetermination Under the ) DECISION AND RECOMMENDATION  
Sales and Use Tax Law: )  
)  
Y--- -. B--- ) No. SR -- XX XXXXXX-010  
dba B--- M--- COMPANY )  
)  
Petitioner )

This petition was heard on Tuesday, July 11, 19XX, at 2:30 p.m. in Hollywood, California, by Hearing Officer Donald J. Hennessy.

Appearing for Petitioners:

S--- -. W---, Tax Counsel and Assistant  
General Counsel for M---, Inc.

Appearing for the Board:

Jan K. Ishii, District Principal Auditor

Edward O. Stewart, Auditor

Protested Item  
(Audit Period 1/1/XX to 6/30/XX)

Petitioner protests a Notice of Determination dated January 7, 19XX, for tax and interest in the total amount of \$X,XXX.XX. A reaudit was performed after the issuance of the determination. Petitioner now specifically protests the entire remaining measure (\$YY,YYY) of tax on the reaudit report dated December 13, 19XX. The measure of tax is for out-of-state sales that have been disallowed due to in-state delivery not supported by bills of lading.

### Contention of Petitioner

All of the questioned transactions were exempt from sales tax as sales in interstate commerce or export sales.

### Summary of Petition

Petitioner is an individual proprietor engaged in the manufacture and sale of industrial molds. There was no prior sales or use tax audit.

The transactions in question here are sales of molds to M---, Inc. (M---), a major --- maker. Petitioner considered such sales as exempt from sales tax as sales in interstate commerce or export sales. The auditor considered such sales as subject to sales tax. No resale certificates were issued by M--- to Petitioner.

Petitioner sent the molds it had manufactured for M--- to an unrelated extruder hired by M--- for shot sampling. The shot sampling produced sample parts to ascertain whether the mold met M---'s specifications. The mold would be returned to Petitioner for correction if it did not meet specifications. Petitioner did not do any shot sampling itself. M---'s purchase orders specifically provided that title to the molds passed to M--- at the F.O.B. point designated on the order but only after inspection and acceptance of the molds by M---.

When the mold was satisfactory, it was picked up at the extruder's place of business by an export packer or a carrier hired by M--- and exported or shipped in interstate commerce. The export packer or carrier received the mold at Petitioner's place of business if the mold had been returned to Petitioner by the extruder. The auditor initially disallowed all such transactions and a meeting was held with Mr. W---, who raised certain questions which resulted in the audit staff requesting an opinion from the legal staff.

The opinion was issued on August 15, 19XX, and a copy was given to Mr. W---. A reaudit applied the guidelines from the opinion and reduced the measure of tax from \$XX,XXX to \$YY,YYY consisting of seven (7) sales of molds to M---. Of the seven sales still in question, the summary prepared by the Board's petition unit notes that: (1) Four sales were disallowed for lack of evidence of delivery by Petitioner to an export packer, with the assumption being that the extruder delivered to the export packer; (2) Two sales were disallowed because Petitioner delivered to the extruder and there is no evidence the mold was ever shipped out of state; and (3) One sale was disallowed because the mold was never shipped out of state. (This last transaction is clearly taxable and shall not be further discussed.

### Analysis and Conclusions

As our main task here is to review the guidelines in the legal opinion of August 15, 19XX, we quote here the summary paragraphs of the opinion.

“In the ultimate summary of all this, we are of the opinion that where taxpayer delivers the molds to an export packer, sales tax will not apply. It is irrelevant that title may have passed previously to the purchaser, and it is irrelevant that taxpayer or taxpayer’s subcontractor or an extruder hired by M--- may have tested the molds. Where taxpayer delivers the molds to a carrier for interstate shipment, the molds will be regarded as having been delivered to the purchaser or his representative where the goods are first sent to an extruder hired by M--- unless the contract of sale requires taxpayer to ship the goods to an out-of-state point.

“Sales tax will apply where taxpayer delivers the molds to an extruder hired by M--- and the extruder delivers the molds to an export packer or to a carrier for interstate shipment.”

These guidelines must be compared to Sales and Use Tax Regulation 1620 (Title 18, Calif. Administrative Code) which is the Board’s implementation of the Interstate Commerce Clause and Export Clause from the United States Constitution and the case law construing those clauses. The guideline that sales tax will not apply when Petitioner delivers the mold directly to an export packer is correct. This result follows from Regulation 1620)(a)(3)(C), which in turn is based on Section 6387 (Revenue and Taxation Code; all section references hereinafter are to such code unless otherwise noted), which specifically exempts sales when delivery is to an export packer. The shot sampling by the extruder does not constitute a “use” (Sections 6009 and 6009.1) whether or not the extruder was hired by M---. In fact, even if the mold was temporarily transferred to M--- solely for testing, the export exemption would still apply, provided the mold was returned to Petitioner and delivered to the export packer by the Petitioner. The Board staff can, of course, require reasonable documentation of Petitioner’s delivery to the export packer. Four of the seven sales here are not allowed as export sales because of the lack of such documentation. We agree with such disallowance.

The second guideline is that, if Petitioner delivered the mold to an extruder hired by M--- and the extruder returned the mold to Petitioner who then delivered to a carrier, the sale by Petitioner will be exempt from sales tax as a sale in interstate commerce only if the contract of sale required Petitioner to ship the mold to an out-of-state point. More simply stated, this guideline requires Petitioner, at the time he transfers possession of the mold to the extruder, to be under an obligation to ship the mold in interstate commerce if the mold is returned to him, and he must actually so ship the mold. The two sales here which are not allowed as sales in interstate commerce must be sustained as audited, even without the application of this guideline, because there is no evidence the molds were ever shipped out-of-state. Again, the Board can require reasonable documentation of any exemption.

But if there was documentation here establishing that Petitioner delivered the molds to a carrier for shipment out-of-state, we believe that the interstate commerce exemption would apply. Therefore, we change the result under the second guideline.

Three factors lead to this change. First, under the title clauses which are part of the contract of sale here, title passes at the F.O.B. point, but only after acceptance by M---. The molds would not be returned to Petitioner unless there was some correction needed which made them unacceptable. Therefore, no sale would occur prior to the correction and delivery by Petitioner to the carrier. Secondly, any acceptance given at the extruder's would be revoked on discovery of the defect, with title reverting in Petitioner pursuant to U.C.C. Section 2401. Thirdly, given the ongoing nature of such sales between M--- and mold makers, it seems clear that often the delivery term of the contract is left open until the mold is satisfactory. It is implied in the contract of sale that the mold maker will ship the mold to wherever M--- instructs. Such instructions (delivery term) are given prior to delivery at the F.O.B. point by Petitioner and, therefore, delivery should be seen as "... pursuant to the contract of sale..." within Regulation 1620.

The third and last guideline here is that sales tax applies to Petitioner's sales when the extruder delivers the mold to the export packer or carrier. Again, this result is required by Regulation 1620. As to the alleged export sales, the case law supporting the regulation is clear. Petitioner's delivery to the extruder did not mark the physical entry of the molds into the stream of exportation by being delivered on shipboard for delivery abroad or to a common carrier for such foreign transportation in a continuous route or journey. (Farmer's Rice Cooperative v. County of Yolo, 14 Cal. 3d 616.) Even if Petitioner delivered to a common carrier for shipment to the extruder, and the extruder delivered to the export packer after testing, Petitioner's sale was not an exempt export. "We find no high authority where delivery to a common carrier for purely intrastate transportation has, as here suggested, been held to trigger the process of exportation." Farmer's Rice Cooperative, supra, at page 626. (cf., Gough Industries v. State Board of Equalization, 51 Cal. 2d 746.)

Situations in which the extruder delivers to a carrier for interstate shipment brings us back to the reasoning of the second guideline. Petitioner never does make delivery to an interstate carrier. In hindsight, Petitioner's obligation as to these molds was completed on delivery to the extruder and Petitioner has no idea whether the molds are ultimately shipped in interstate commerce. Therefore, the tax applies as in Regulation 1620(a)(3)(A).

#### Recommendation

Petition Unit is to reduce the measure of tax to the \$YY,YYY shown in the reaudit report dated December 13, 19XX, and redetermine without other change.

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Donald J. Hennessy, Hearing Officer

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Oct. 2, '78  
Date