

**STATE BOARD OF EQUALIZATION**

1020 N STREET, SACRAMENTO, CALIFORNIA
(P.O. BOX 942879, SACRAMENTO, CALIFORNIA 94279-0001)
(916) 445-5550

January 7, 1991

Mr. J--- M. L---
P--- & M---
Attorneys at Law
XXX --- Street
--- ---, California XXXXX

RE: The H--- Corporation
SZ -- XX-XXXXXX

Dear Mr. L---:

This is in response to your letter dated December 6, 1990, regarding the application of sales tax to the business of your client, The H--- Corporation.

H--- fabricates structural steel and acts as a construction contractor throughout the United States. H--- is planning to enter into a new line of business in which it sells its fabricated steel to other construction contractors. A portion of those sales will be for export to foreign countries.

H--- purchases steel and other raw materials (such as weld wire and flux) for use in fabricating the steel. Although the steel is purchased from the manufacturer on a project-by-project basis, the other raw materials are purchased in bulk and a determination cannot be made by H--- at the time of purchase as to how much of the materials will eventually be used for fabricating steel for resale. Under H---'s accounting system an estimate is made of the cost of such materials to be used for each steel fabrication job, and the estimate is charged to the job as the fabrication process progresses. H--- uses this same accounting system to allocate the cost of raw materials charged to each steel fabrication job regardless of whether the finished product will be used in its own construction business or will be resold.

When H--- sells fabricated steel for export, the steel will be delivered to a customs broker or common carrier F.O.B. California. When H--- makes the shipping arrangements, it will obtain copies of the marine insurance policy and bill of lading which indicates the foreign destination. When the shipping arrangements are not made by H---, H--- will require that its customer furnish similar documentary evidence showing that the destination of the fabricated steel is outside the United States.

You ask that we render three opinions. Each of your requested opinions is quoted below followed by our response.

“(1) The purchases of steel and other raw materials by H---, which materials are combined during the fabrication process and exported by H--- in the form of fabricated steel, where H--- has no responsibility for the erection of the steel, will not be subject to sales or use tax in California.”

Sales or use tax is applicable to the sale and purchase of tangible personal property at retail. (Rev. & Tax. Code §§ 6051, 6201.) A retail sale is a sale for any purpose other than resale in the regular course of business. (Rev. & Tax. Code § 6007.) H--- will be regarded as purchasing property for resale when it incorporates such property into the fabricated steel without prior use and resells that fabricated steel without using it. H--- may purchase such property ex-tax for resale. (Reg. 1668.) However, it appears that at least some of the raw materials may actually be purchased for use by H--- in the manufacture of its fabricated steel and not for resale. For example, chemicals used as catalysts or otherwise to product a chemical or physical reaction such as the production of heat or removal of impurities may not be purchased for resale even if some of those chemicals are incidentally incorporated into the finished product. (Reg. 1525(a). See Annot. 440.1740 (5/16/52).) Flux may be used as a cleansing agent or as a means of reducing oxidation. If used in this manner, it is regarded as consumed in the manufacture of the fabricated steel and H--- may not purchase the flux ex-tax for resale. On the other hand, flux may be used for transmitting desirable alloys from the flux to the metal. If H--- purchases the flux for this purpose, the flux may be purchases ex-tax for resale.

“(2) The accounting method used by H--- constitutes sufficient evidence to support a claim for a ‘tax-paid purchases resold’ deduction on H---’s sales tax return for sales tax paid on raw materials used in the fabrication of steel that is resold.”

As discussed above, it is not clear that all raw materials about which you inquire may be purchased by H--- for resale. With respect to the materials that H--- purchases for the purpose of incorporating them into the final product that will be resold, H--- may take a tax-paid purchases resold deduction with respect to sales tax reimbursement or use tax paid when purchasing those materials. H---’s accounting system for taking the tax-paid purchases resold deduction appears acceptable. However, this is an auditing question that you may wish to direct to Mr. Glenn Bystrom, Principal Auditor, at the address above.

“(3) Sales of fabricated steel by H--- for export, where H--- has no responsibility for the erection of the steel, will not be subject to sales or use tax in California if H--- receives documentary evidence in the form of bills of lading and marine insurance policies, whether or not H--- is responsible for making arrangements for the transportation of the steel.”

Revenue and Taxation Code section 6396 exempts from sales tax the sale of tangible personal property which, pursuant to the contract of sale, is required to be shipped and is shipped to a point outside this state by the retailer by means of: facilities operated by the retailer; or delivery by the retailer to a carrier, customs broker or forwarding agent, whether they are hired by the purchaser or not, for shipment to such out-of-state point. (See also Regulation 1620.) We note that this exemption applies not only to sales made for delivery to other countries which meet the requirements of the exemption, but also to sales for delivery to other states when those sales meet the requirements of the exemption. When the contract of sale requires shipment of the steel to a point outside this state by the retailer and H--- delivers the property to the common carrier or customs broker for shipment outside this state while retaining documentary evidence in the form of bills of lading and marine insurance policies, no sales tax will apply whether or not H--- is responsible for making arrangements for the transportation of the steel. However, please note that this exemption applies only when the purchaser does not obtain possession of the purchased property in this state. That is, H--- must delivery the property to the common carrier or customs broker and the property must be shipped outside this state prior to the purchaser gaining possession of that property.

A further note is the presumption set forth in Revenue and Taxation Code section 6247. When a retailer sells property for delivery outside this state to a purchaser known by the retailer to be a resident of this state, it is presumed that the purchaser purchases that property for use in this state. Thus, even though the sale may qualify for the exemption from sales tax provided by Revenue and Taxation Code section 6396, use tax is presumed to apply. This presumption may be controverted by a statement in writing, signed by the purchaser or its authorized representative and retained by the seller, that the property was purchased for use at a designated point or points outside this state. The presumption may also be controverted by other evidence satisfactory to the board that the property was not purchased for use in California. Thus, when a California resident purchases steel from H--- and H--- will deliver the property to a common carrier or customs broker for shipment outside this state, H--- should obtain a certificate from the purchaser that the property will be used outside this state or should collect use tax.

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

Sincerely,

David H. Levine
Senior Tax Counsel

DHL:cs
0081E

bc: Mr. Glenn Bystrom
San Francisco District Administrator

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1020 N STREET, SACRAMENTO, CALIFORNIA
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January 17, 1991

Mr. J--- M. L---
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Attorneys at Law
XXX --- Street
--- ---, California XXXXX

RE: The H--- Corporation
SZ – XX-XXXXXX

Dear Mr. L---:

This is in response to your letter dated January 10, 1991. In a letter dated January 7, 1991, I responded to your previous letter concerning the application of sales and use tax to the business of your client, The H--- Corporation. You now state:

“In your analysis of the third option requested, you state that the exemption for export sales applies only when the purchaser does not obtain possession of the purchased property in California. I would like to confirm that you do not intend to suggest that the purchaser may not obtain title while the property is located in California, only that the purchaser may not obtain possession.”

The subject exemption is an exemption from sales tax for property shipped outside the state pursuant to the contract of sale. Sales tax applies only to sales occurring in California. (Rev. & Tax. Code §§ 6006, 6051.) Thus, when title transfers outside California, the sale does not occur inside California and no sales tax applies. (But see Commercial Code § 2401, Reg. 1628(b)(3)(D) (title passes no later than when the retailer completes his performance with reference to the physical delivery of the property and any title retained is merely a security interest).) Only when sales tax would otherwise apply is it necessary to ascertain whether a sale qualifies for the exemption provided by Revenue and Taxation Code section 6396. In other words, the exemption specifically applies to qualifying sales occurring inside California.

In summary, the short answer to your request for confirmation is that your understanding is correct. If the sale satisfies the requirements of the exemption, the exemption applies even though title is transferred and the sale occurs inside California. I note that the obtaining of possession by the purchaser that eliminates the exemption includes any transfer of the

subject property to a third person except the specific persons for the specific purpose indicated in the exemption (a carrier, customs broker, or forwarding agent for shipment outside California). For example, if the seller transferred the subject property to a third person for storage prior to shipment, the sale occurs in California and does not qualify for the exemption.

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

Sincerely,

David H. Levine
Senior Tax Counsel

DHL:cs
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