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April 17, 1997

Ms. A--- G---
S--- C---
Chartered Accountants
XX --- ---
Suite XXXX
---, ---, --- ---, Canada

Re: Unidentified Taxpayer

Dear Ms. G---:

This is in response to your letter dated March 12, 1997 regarding the application of sales tax to a transfer between related entities. Initially I note that you have not identified your client. As such, this is not a letter on which your client may rely within the provisions of Revenue and Taxation Code section 6596.

You state that two individuals (A and B) and a corporation (C) own a limited liability company (LLC). You state that the same owners also own another company (Company) in the same proportion, except that A and B own their interests through a different corporation (Holding). Company will form a wholly-owned subsidiary (Newco). Newco will then purchase all the assets of LLC. You ask whether the sale from LLC to Newco qualifies as an exempt occasional sale.

You do not state the proportion of ownership of these entities, nor have you indicated whether Company is a corporation. For purposes of this opinion, I assume that Company is a corporation. I assume that each of the three owner-members of LLC, A, B, and C, owns a one-third interest in LLC. I also assume that A and B each own one-half of the stock of Holding, and that C owns one-third and Holding owns two-thirds of the stock of Company.

Revenue and Taxation Code section 6367 provides an exemption for occasional sales. Subdivision (b) of Revenue and Taxation Code section 6006.5 defines an “occasional sale” to include:

“Any transfer of all or substantially all the property held or used by a person in the course of those activities when after the transfer the real or ultimate ownership of the property is substantially similar to that which existed before the transfer. For the purposes of this section, stockholders, bondholders, partners, or other persons holding an ownership interest in a corporation or other entity are regarded as having the ‘real or ultimate ownership’ of the property of the corporation or other entity.”

Although the exemption provided by section 6367 excludes sales of vehicles, vessels, or aircraft, Revenue and Taxation Code section 6281 provides a similar exemption for sales of such property:

“There are exempted from the taxes imposed by this part the gross receipts from the sale of, and the storage, use, or other consumption in this state of, a mobilehome or commercial coach required to be annually registered under the Health and Safety Code, or a vehicle required to be registered under the Vehicle Code or subject to identification under Division 16.5 (commencing with Section 38000) of the Vehicle Code, or a vessel or aircraft, when such property is included in any transfer of all or substantially all the property held or used in the course of business activities of the person selling the property and when after such transfer the real or ultimate ownership of such property is substantially similar to that which existed before such transfer. For the purposes of this section, stockholders, bondholders, partners, or other persons holding an interest in a corporation or other entity are regarded as having the ‘real or ultimate ownership’ of the property of that corporation or other entity.”

When a seller transfers all its property, as will LLC, then the sale will qualify for the exemption under section 6281 or section 6367, or both, if after the transfer the “real or ultimate” ownership of the transferred property is substantially the same as before the transfer. (See Reg. 1595.) Under the facts stated in your letter and the assumptions set forth above, tracing ownership through the chain of ownership of the participants, A, B, and C each owns one-third of LLC and each also owns one-third of Company; A, B, and C will also each own one-third of Newco using the “tracing” method of analysis. Thus, if the tracing method of analysis is correct, for purposes of the occasional sale exemption A, B, and C each owns a one-third interest in the property to be transferred by LLC and will each own the same interest in that property after the transfer. On the other hand, if there is no tracing through the levels of ownership, A, B, and C will have no ownership interest the property after the transfer, nor will LLC. The question, therefore, is whether the exemptions contemplate determining ownership only of the person

selling the property and the person purchasing the property, or do they contemplate tracing ownership through multiple levels of the ownership (e.g., the “grandparent” of the seller and the “great grandparent” of the purchaser).

As you might imagine, this is not a new question. We have concluded that the exemptions do contemplate an analysis of common ownership. (BTLG Annot. 395.2540 (6/29/54).) The analysis is performed on a parent-child basis (as opposed, obviously, to a sibling relationship). For example, if a tracing of the seller’s lineage through to its great grandparent and a tracing of the purchaser’s lineage through its great grandparent leads to the same person, the ownership will be regarded as the same before and after the transfer, even if a tracing through only the grandparents would reveal no common ownership between the seller and the purchaser. Thus, we conclude that the proposed transaction will qualify as an occasional sale and will be exempt from sales and use tax.

You also note that some of the persons identified above are Canadian, and you ask whether this is relevant. If a person sells substantially all its property to a person with substantially the same ownership, the transaction will qualify for the exemption without regard to whether the buyer or seller, or both, or any of the “real or ultimate” owners of them are not residents of California.

Please note that the conclusion reached above applies only to the specific facts and assumptions stated above. If you have further questions, feel free to write again.

Sincerely,

David H. Levine
Supervising Tax Counsel

DHL/cmm

cc: Out-of-State District Administrator (OH)
Mr. Vic Anderson (MIC:38)
Mr. Robert Nunes (MIC:40)