

**STATE BOARD OF EQUALIZATION**

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May 19, 1993

Mr. E--- R. H---
---, --- & ---
Certified Public Accountants
XXX --- Avenue
--- ---, NY XXXXX

Dear Mr. H---:

This is in response to your letter dated April 15, 1993 in which you state:

"I am the accountant for a New York client that has a warehouse in California. Much of their product is sold to the ultimate consumer and California sales tax is charged on shipments in California. Some of the product is shipped from the California warehouse, and a large volume of product is drop shipped from out of state to California customers.

"The client has a customer in the linen rental business and the customer has plants inside and outside California and a receiving warehouse in California.

"The customer has requested my client to ship merchandise from client warehouse in California and from out of state sources to the customer warehouse in California and not charge them sales tax. The reason for this is that the customer is shipping part of the merchandise to their plants out of California. For the merchandise being used in California, it is not immediately put in service.

"The merchandise shipped from client's California warehouse and out of state sources are identical in many instances, and the customer probably does not know, in advance, where the merchandise will be used. It is the customer's contention that the tax for merchandise used in California becomes payable when it is removed from the warehouse and put in circulation.

"They are reporting and paying use tax only on the merchandise used in California when it is taken out of the warehouse. This same customer advised my client that they have received permission for this procedure from the State Board of Equalization office in Colton, California. The customer has offered to provide our client with a resale certificate."

Revenue and Taxation Code section 6051 imposes a sales tax on all retailers measured by their gross receipts from retail sales of tangible personal property. Sales tax applies to sales occurring in California. There is no exemption from sales tax where the purchaser takes possession of the property in California and subsequently removes the property out-of-state. This is true even if no use other than storage and removal is made by the purchaser and the purchaser intends at the time of sale to remove the property outside of California. Pope v. State Board of Equalization (1988) 202 Cal. App. 3d 73 and Eng Motor Truck Company v. State Board of Equalization (1987) 189 Cal. app. 3d 1458.

Revenue and Taxation Code section 6201 imposes an excise tax, commonly referred to as the use tax, on the storage, use, or other consumption in this state of tangible personal property purchased from any retailer for storage, use, or other consumption in this state. The use tax complements the sales tax and is imposed upon out-of-state purchases of property for use in California. Thus, if a purchaser orders property from a retailer who ships the property from an out-of-state point to California, the transaction is subject to use tax, not sales tax.

The use tax is imposed upon the purchaser, but if a retailer is engaged in business in California and makes sales of tangible personal property for storage, use, or consumption in this state, he or she must, at the time of making the sale, collect the use tax from the purchaser and pay it to the state. Rev. & Tax. Code § 6203.

"Storage" and "use" do not include the keeping, retaining, or exercising any right or power over tangible personal property for the purpose of subsequently transporting it outside the state for use thereafter solely outside the state, or for the purpose of being processed, fabricated, or manufactured into, attached to or incorporated into, other tangible personal property to be transported outside the state and thereafter used solely outside the state. Rev. & Tax. Code § 6009.1. This exclusion is for use tax transactions, not sales tax transactions.

Sales tax applies only to retail sales. A "retail sale" or "sale at retail" means a sale for any purpose other than resale in the regular course of business in the form of tangible personal property. Rev. & Tax. Code § 6007. Use tax does not apply to transactions in which the purchaser purchases the property for resale and makes no use of the property other than retention, demonstration, or display while holding the property for sale in the regular course of business. Rev. & Tax. Code § 6244.

A person who makes a sale of tangible personal property has the burden of proving that the sale is not a sale at retail or that the property sold for delivery in this state was not purchased for use in California unless he or she takes from the purchaser a resale certificate. Rev. & Tax. Code §§ 6091 and 6241. However, the certificate relieves the seller from liability only if taken in good faith from a person who is engaged in the business of selling tangible personal property and who holds a seller's permit. Rev. & Tax. Code §§ 6092 and 6242. If the seller knows that the purchaser is not purchasing the property for resale, the seller cannot take the certificate in good faith and is therefore not relieved from liability by the certificate.

With respect to the facts you gave, the application of tax is as follows:

As you are aware, a "sale" and "purchase" do not include a lease of linen in which an essential part of the lease agreement is the furnishing of recurring service of laundering. Rev. & Tax. Code §§ 6006(g)(2) and 6010(e)(2). Therefore, the client's customer is not purchasing the linens for resale, and your client cannot accept a resale certificate from the customer in good faith.

Sales of all merchandise which is shipped from your client's California warehouse to the customer's warehouse in California are subject to sales tax since the sales occur in California. This includes merchandise which is subsequently shipped by the customer to its out-of-state business locations. As noted above, the exclusion from tax under section 6009.1 does not apply because these are sales tax transactions. The sales tax is imposed upon your client though the client may, by contract, collect sales tax reimbursement from the customer. Civ. Code § 1656.1.

Use tax applies to those transactions in which merchandise is shipped from out-of-state suppliers to the customer's California warehouse and is used at the customer's California business locations. Since your client is engaged in business in California, your client is obligated to collect the use tax from the customer and pay it to the state.

Use tax does not apply to those transactions in which merchandise is shipped from out-of-state suppliers to the customer's California warehouse, is never used in California, and is subsequently transported to the customer's out-of-state business locations for use solely outside of California. If a purchaser knows that specific property will meet the requirements of the section 6009.1 exclusion, the purchaser may issue to the seller an exclusion certificate in the sample form we have enclosed.

The problem in this case is that the customer does not know in advance which linens it receives from the out-of-state suppliers will be used in California and which will be shipped to outside business locations. Therefore, the customer may not purchase linens from out-of-state suppliers ex tax by issuing an exclusion certificate since not all of linens will be removed from the state. The matter is further complicated by the fact the customer commingles linens purchased out-of-state with linens purchased in-state.

To solve these problems the customer should keep updated records showing what percentage of its linens are purchased from out-of-state and what percentage of its linens are purchased in-state. When the customer sends linens out-of-state, the customer may file a claim for refund for use tax. The measure of the refund is calculated by multiplying the percentage of out-of-state inventory at the time the linens are removed from the state times the total purchase price of the linens removed from the state. For example, if at the time of removal 60 percent of the customer's inventory is from out-of-state suppliers and the total purchase price of the linens removed from the state is \$5,000, the customer would be entitled to a refund calculated by multiplying the tax rate times \$3,000 (60% of \$5,000).

Revenue and Taxation Code section 6596 provides the only basis for relief from tax if a taxpayer relies on incorrect written advice from the board. The primary conditions to qualify are that the request for opinion must be in writing and must disclose all relevant facts, including the identity of the taxpayer. Since you have not identified your client, this opinion does not come within the provisions of section 6596 but rather is simply general advice regarding a set of hypothetical facts.

If you have further questions regarding Sales and Use Tax Law, please do not hesitate to write again.

Sincerely,

Elizabeth Abreu
Tax Counsel

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Enclosure