

**STATE BOARD OF EQUALIZATION**

1020 N STREET, SACRAMENTO, CALIFORNIA
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October 4, 1990

Ms. L--- S. O---
Manager, Contracts
A--- O--- A---
 Incorporated
XXX --- Road, Bldg. ---
--- ---, CA XXXXX-XXXX

SR -- XX-XXXXXX

Dear Ms. O---:

Jean McNeill of the Return Review Unit has forwarded to the legal staff your letter of July 17, 1990 to the State Board of Equalization, and I have been assigned to respond. As I understand it, the issue is whether the original purchase order discussed below qualifies for an exemption from the additional ½% San Diego Transactions and Use Tax, which was enacted effective January 1, 1989.

I. FACTUAL BACKGROUND

You set forth the problem as follows:

“A--- O--- A--- (hereinafter ‘O---’) received a fixed price purchase order (No. G98025) from the University of California, San Diego on December 9, 19XX for equipment with scheduled deliveries in June and July of 1989. The purchase order was funded for \$XXX,XXX plus sales tax at 6.5%. With the purchase order we received a deposit check which was held in a deposit account and reversed into a sales account with the first shipment. At that time, we invoiced the second installment payment. Final shipment and invoicing were made in July of 1989. A copy of the purchase order is attached. It should be noted that this purchase order was issued to us for equipment required by S--- I--- for their performance under Federal Government Contract No. N00014-87-K-0120.

“On May 25, 1989, we received an amendment to the purchase order to include additional equipment. This amendment reflected the new 7% sales tax. A copy of this amendment is also enclosed.”

The documents you attached showed the rate and amount of sales tax (6.5%, \$19,524.18) which was included in the total price. The payment terms included a requirement that 35% of the total be included with the purchase order as a down payment. There was a hand-written notation: “Cheque No. 3-56164 attached herewith (\$111,963.66” [sic]. I assume that this check is the deposit to which you refer in you letter. The requisition date was November 21, 1988; the confirming date was December 9, 1988; and the delivery dates were 6/28/89-7/28/89.

The documents appear to be the vendor’s copies of the purchase order. They do not include a written acceptance of the order, or any other documentary evidence that O--- agreed to be bound by the order.

The documents also do not indicate that either O--- or its purchaser claim that the sales are exempt as being to the United States.

II. OPINION

A. Transactions and Use Tax Generally

In 1969, the Legislature enacted the Transactions and Use (hereinafter “District”) Tax Law. (Rev. & Tax. Code §§ 7251ff. All further statutory references are, unless otherwise stated, to the Revenue and Taxation Code.) The San Diego Regional Transportation Commission, and county regional justice facilities financing agencies were defined as “districts” for which the District tax could be imposed. (§§ 7252.7, 7252.15.) To support such districts, sales and use taxes could be imposed at the rate of up to 0.5% of the gross receipts from the sale of tangible personal property sold at retail or of the sales price of property whose use, storage, or consumption is subject to tax. (§§ 7261(a)(1), 7262(a).)

The San Diego County voters approved a District tax operative April 1, 1988, to support the Regional Transportation Commission. The voters approved a like tax operative January 1, 1989, to support the Regional Justice Facilities Financing Agency, increasing the total rate effective in San Diego County to 7%.

B. Exceptions to the District Tax

There are some exceptions to the District tax. Sections 7261(8) and 7262(a)(6), implemented by Regulations 1823(a)(2)(C) and 1823(b)(2)(C), provide that a sale, storage, use or other consumption of tangible personal property is exempt from the tax if the seller is obligated to

furnish or the purchaser is obligated to purchase the property for a fixed price prior to the operative date of the ordinance imposing the tax.

C. What is a Binding Contractual Obligation?

“A contract is an agreement to do or not to do a certain thing.” (Civ. Code § 1549.) For a contract to be binding, there must be parties capable of contracting, their consent, a lawful object, and a sufficient consideration. (Civ. Code § 1550.)

The parties’ consent is manifested by an offer or proposal and the offeree’s acceptance of the same. (Sackett v. Starr (1949) 95 Cal.App.2d 128, 133 [212 P.2d 535]; Civ. Code § 1583.) Where the sale of goods is involved, acceptance does not have to be in any particular form but may be in any manner and by any medium reasonable in the circumstances. (Cal. U. Com. Code § 2206(1).) Performance of the conditions of a proposal or the acceptance of the consideration offered with a proposal, is an acceptance of the proposal. (Estate of Klauenberg (1973) 32 Cal.App.3d 1067, 1070 [108 Cal.Rptr. 669]; Civ. Code 1584.)

The regular practice between the buyer and seller can flesh out the terms of a contract. (Southern Cal. Acoustics Co. v. C. V. Holder, Inc. (1969) 71 Cal.2d 719, 722 [79 Cal.Rptr.319, 456 P.2d 975].) In a shipment contract, shipment of the goods pursuant to the terms of the purchase order is a reasonable mode of acceptance of the offer—i.e., the purchase order. (In the Matter of Isis Foods, Inc. (Bky. W.D. Mo., W.D., 1983) 38 B.R. 48, 49.)

D. Tax Consequences to O---

In determining whether a sales contract is a “fixed-price” contract for the purpose of the district tax, we have consistently required that it satisfy the following criteria: (1) it be binding prior to the operative date of the ordinance establishing the tax; (2) neither party has an unconditional right to terminate the contract; and (3) the amount of tax or the tax rate is set forth in the contract. Change orders are regarded, however, as new contracts. If they are executed after the operative date of the ordinance, they are subject to the new tax.

Was the contract at issue binding prior to January 1, 1989? The documents give us the names of the parties, recite the consideration, and appear to encompass a legal sale. They do not, however, indicate that O--- considered itself bound by the purchase order prior to January 1, 1989. It is true that O--- shipped in accordance with the order, but only after the operative date of the tax ordinance. We do conclude, however, that by placing the purchaser’s check in its deposit account, O--- accepted the consideration for the purchase order and so became bound to the contract prior to January 1, 1989.

The purchase order set forth both the amount and rate of tax, calculated at the rate in effect in San Diego County prior to January 1, 1989. Article 4(a.) of the Terms and Conditions shows that O--- could make changes only with the written consent of the purchaser and the purchaser could terminate the contract only upon full payment for goods already shipped or by payment of a reasonable amount for goods not shipped which O--- could not recover from other sources. (See, Cal. U. Com. Code § 2703.) We conclude that this is not the type of unconditional termination clause which would disqualify a fully-executed sales contract from being termed a "fixed-price" contract as defined above.

Since the amendment to the purchase order was received after January 1, 1989, it was rightly subject to the new rate.

III. CONCLUSION

In short, we conclude that, since O--- accepted the consideration which the purchaser paid pursuant to the terms of the purchase order, a binding contract came into being as of December 9, 1988. The tax rate and amount were set forth, and neither party had an unconditional right to terminate the contract. Therefore, this contract meets the definition of a "fixed-price" contract as described above. It is subject to the District tax rate of 6½% effective in San Diego County on the date of acceptance, December 9, 1988. Since the amendment was received after January 1, 1989, it was rightly subject to the new 7% rate.

I have enclosed a copy of Regulation 1823 for your information. If you have any further questions, please do not hesitate to write again.

Very truly yours,

John L. Waid
Tax Counsel

JLW:sr

Enc.

bc: --- District Administrator