



STATE BOARD OF EQUALIZATION

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October 6, 1992

BURTON W. OLIVER
Executive Director

Mr. J--- D. B---
S--- D---, Inc.
P. O. Box XXXX
--- ---, CA XXXXX-XXXX

Re: SR -- XX-XXXXXX

Dear Mr. B---:

This is in response to your letter dated July 24, 1992, in which you state:

"Our company is currently being audited by the Board of Equalization in order to determine our compliance with California sales & use tax law. The state has asserted that certain sales made to out of state customers that were delivered to in state sub-contractors designated by the customer are taxable. It is our understanding that possible future questions regarding the application of sales taxes to such sales may be avoided by adding the following statement to our customer order acknowledgments as an additional term and condition of the sale.

"Special note for customers located outside the State of California: If your order requires cotton knit backing, and you do not choose the contractor to perform this work, SDI will designate the sub-contractor and retain ownership of the goods through completion of this backing process. You the customer will pay SDI's sub-contractor directly for the cotton knit backing process. Delivery of these backed goods to any point located within the State of California will result in SDI adding California sales tax to the sale, unless SDI is provided a valid California resale card and the goods are being purchased for resale.

"California sales tax must apply to this sale if these conditions are not met.

"SDI will not be responsible for goods that are lost or damaged by a contractor that you choose."

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. All gross receipts from sales of tangible personal property are presumed taxable until the contrary is established. Rev. & Tax. Code section 6091. Although the sales tax is imposed upon the retailer, the retailer may collect sales tax reimbursement (usually itemized on the invoice as "sales tax") from the purchaser if the contract of sale so provides. Civ. Code § 1656.1.

Revenue and Taxation Code section 6396, which provides an exemption from sales tax for certain interstate shipments, reads:

"Interstate shipments. There are exempted from the computation of the amount of the sales tax the gross receipts from 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: (a) facilities operated by the retailer, or (b) delivery by the retailer to a carrier, customs broker or forwarding agent, whether hired by the purchaser or not, for shipment to such out-of-state point.

"For purposes of this section, the term 'carrier' shall mean a person or firm engaged in the business of transporting for compensation tangible personal property owned by other persons, and includes both common and contract carriers. The term 'forwarding agent' shall mean a person or firm engaged in the business of preparing property for shipment or arranging for its shipment."

Regulation 1620(a)(3)(A) provides:

"To Other States--When Sales Tax Applies. Except as otherwise provided in (B) below, sales tax applies when the property is delivered to the purchaser or the purchaser's representative in this state, whether or not the disclosed or undisclosed intention of the purchaser is to transport the property to a point outside this state, and whether or not the property is actually so transported. It is immaterial that the contract of sale may have called for the shipment by the retailer of the property to a point outside this state, or that the property was made to specifications for out-of-state jobs, that prices were quoted including transportation charges to out-of-state points, or that the goods are delivered to the purchaser in this state via a route a portion of which is outside this state. Regardless of the documentary evidence held by the retailer (see (3)(D) below) to show delivery of the property was made to a carrier for shipment to a point outside the state, tax will apply if the property is diverted in transit to the

purchaser or his representative in this state, or for any other reason it is not delivered outside this state."

In your case, the broad issue is whether certain sales to your customers are exempt under this section. If the property is delivered to your customer or its representative at a California location, the sale is not exempt from tax under section 6396. The specific issue raised by your letter is whether a contractor who adds cotton knit backing is a representative of the customer or a representative of S--- D---. If the contractor is a representative of the customer, the interstate shipment exemption does not apply if the contractor is located in California because the retailer has not shipped the property to an out-of-state point. If the contractor is solely the representative of S--- D---, then shipment by the contractor to an out-of-state point is considered shipment by S--- D--- to an out-of-state point and the exemption applies.

Where the customer contracts with the contractor to add knit backing, the contractor is the customer's representative. If S--- D--- contracts directly with the contractor, the contractor will be considered its representative only if all of the following conditions are met:

1. S--- D--- must be responsible for paying the contractor directly or must be liable for payment to the contractor if the customer fails to make payment to the contractor.
2. S--- D--- must be liable to the customer for losses, breach of contract, or damages caused by the contractor. However, whether S--- D--- can look to the contractor for indemnification is a matter of contract between them and would not effect the application of tax.
3. The contractor must be solely S--- D---'s representative. In other words, the contract must not state or imply that the contractor is the agent, independent contractor, or other type of representative of the purchaser.

We are confused by the statement you propose to include on S--- D---'s customer order acknowledgements. Contract provisions cannot shift the incident of sales tax from one party to another or change a taxable transaction into a nontaxable transaction. Thus, if a contract is subject to tax, S--- D--- cannot avoid the imposition of sales tax if it fails to collect sales tax reimbursement from the customer because the parties mistakenly believed that the contract was not subject to tax.

Since all gross receipts from retail sales are presumed taxable, S--- D--- will have the burden of establishing that the interstate shipment exemption applies. If S--- D--- does not have a written contract with the contractor or if the terms of its written contracts are unclear, it may not be able to establish that it is entitled to the exemption, particularly if the purchaser designates

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the contractor or title passes to the purchaser prior to delivery of the merchandise to a common carrier by the contractor or title passes to the contractor.

In sum, unless S--- D--- is provided with a timely and valid California resale certificate which it takes in good faith, S--- D--- is liable for sales tax on any sale in which delivery of the goods is made to a contractor located in California and the contractor is not solely the representative of S--- D--- as described in this letter.

We are enclosing a copy of Regulation 1620 for your information. If you have further questions regarding Sales and Use Tax Law, please do not hesitate to write again.

Sincerely,

Elizabeth Abreu
Tax Counsel

EA:cl

Enclosure: Regulation 1620