

**STATE BOARD OF EQUALIZATION**

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January 8, 1987

--- [R]
[L]
XXX --- ---
--- ---, CA XXXXX-XXXX

Re: F- --- XX-XXXXXX
S- --- XX-XXXXXX

Dear Mr. [R]:

This is in response to your letter dated December 24, 1986 to Tax Counsel E. L. Sorensen in which you ask for our expedited opinion regarding the measure of sales tax on transactions that result in the sale of businesses.

Five entities are involved in transactions which result in [S] Corporation ("Seller") selling a newly formed corporation, [LGI], to a wholly-owned subsidiary of [G] ("Purchaser"). Seller will transfer the assets of [LG], a division of Seller, and [LT], a wholly-owned subsidiary of Seller, to [LGI] before [LGI] is sold to purchaser.

The assets of [LG] which Seller will transfer to [LGI] consist of cash, receivables, inventory, land, buildings, equipment, vehicles, and other tangible and intangible assets (including governmental licenses and permits). Seller will also transfer the various contractual rights of [LG] described in Exhibit A ("operating agreements").

The assets of [LT] which Seller will transfer to [LGI] consist of cement transport trucks, PUC cement carrier permit, and certain operating agreements described in Exhibit A.

The operating agreements do not involve any liability for goods, services, or money received prior to the time the transfers to [LGI] are closed, although each may involve future obligations arising for future value in the normal course of business.

Seller will liquidate [LT] and, in exchange for all [LGI]'s stock, will transfer to [LGI] substantially all the assets of [LG] and [LT], subject only to certain debts described in Exhibit B ("assumed indebtedness") and future obligations arising under the operating agreements. Seller will

then sell all stock of [LGI] to Purchaser. Except for the assumed indebtedness, Seller will retain all other indebtedness of [LG] and [LT].

Seller is a party to two equipment leases with purchase options covering a dredge and certain concrete mixer trucks which are essential to [LG]'s business. Seller will either exercise the purchase options and pay the purchase prices, or transfer the leases to Purchaser who will then exercise the purchase options and make the equipment available to [LGI]. Sales tax resulting from the exercise of the purchase options will be paid by the buyer (that is, Seller or Purchaser) and you do not request an opinion with regard to the exercise of these purchase options. We therefore do not consider the exercise of these purchase options in this opinion.

You ask us to agree with four statements. I have rephrased your statements and discuss each below.

STATEMENT 1

California sales tax does not apply to the dissolution of [LT] and liquidating distribution of [LT]'s assets to seller.

DISCUSSION

We agree. A liquidating dividend does not constitute a sale under Revenue and Taxation Code (all references to sections are to this code) section 6006. (Business Taxes Law Guide ("BTLG") Annotation 395.2280 (1/3/63).) As a liquidating dividend, the transfer of [LT]'s assets to Seller is not subject to sales tax.

STATEMENT 2

The sales tax applicable to Seller's transfer to [LGI] of the assets held by [LG] and those previously held by [LT] will be measured by the indebtedness of Seller assumed by [LGI]. For purposes of this opinion, the assumed indebtedness listed in Exhibit B constitutes an indebtedness of Seller whereas the operating agreements listed in Exhibit A do not constitute indebtedness of Seller.

DISCUSSION

We agree. The transfer of assets to [LGI] does not qualify as an exempt occasional sale under sections 6006.5, 6281, and 6367. The assets to be transferred are presumably used in the course of activities requiring a seller's permit. Therefore, the transfer is not an occasional sale under section 6006.5(a). The assets transferred to [LGI] presumably are not substantially all the property (80% or more) held by Seller. Therefore, the transaction is not an occasional sale under section 6006.5(b) and is not exempt under sections 6281 and 6367. (Sales and Use Tax Regulation 1595(b) & (c).)

Since the transfer of assets to [LGI] is not exempt, the measure of the sales tax is the consideration received by Seller for the transfer of tangible personal property. (§§ 6012, 6051.) That consideration is the assumed indebtedness. (Reg. 1595(b)(4).) Liabilities incurred under the operating agreements will not be included in the measure of tax to the extent that those liabilities are incurred after the closing and are for benefits received after the closing. However, any liabilities incurred under the operating agreements prior to the date of closing the transfer to [LGI] and any liabilities related to benefits received by [LG], [LT], and Seller prior to closing the transfer to [LGI] will be included in the measure of tax.

STATEMENT 3

The actual measure of the sales tax is the percentage that the fair market value of the tangible personal property transferred bears to the fair market value of all assets transferred, multiplied by the taxable consideration received (that is, the assumed indebtedness).

DISCUSSION

We agree. Only the sale of tangible personal property is subject to sales tax. (§ 6051; see BTLG 395.1040 (3/10/59), 395.1260 (11/12/58).) If tangible personal property is sold along with real estate and intangible property, we determine the percentage that the fair market value of the tangible personal property bears to the fair market value of all assets transferred. That percentage of the consideration received by the transferor is attributed to the transferred tangible personal property and is subject to sales tax.

STATEMENT 4

Sales tax will not apply to the sale by Seller of [LGI] stock to purchaser.

DISCUSSION

We agree. As discussed above, sales tax applies only to the sale of tangible personal property. Stock in a corporation is not tangible personal property for purposes of California sales tax. Therefore, sale of the stock of [LGI] to Purchaser for cash or equivalent (bank to bank transfer, draft, check, etc.) is not subject to sales tax.

If the discussion herein of the restatements of your requests does not answer all your questions, feel free to write us again.

Sincerely,

David H. Levine
Tax Counsel

OPERATING AGREEMENTS

1. Leases of real property and equipment;
2. Construction, materials and supply contracts;
3. Contracts to render or receive services;
4. Contracts to sell or buy goods;
5. Proposals and bids;
6. Collective bargaining agreements, and Employee benefit plans and related Agreements; and
7. Miscellaneous governmental licenses and Permits.

EXHIBIT A

LIABILITIES TO BE ASSUMED

BY [LGI] AT CLOSING

ACCOUNTS PAYABLE

Accts. Payable – Deferred
Association Dues
San Gabriel Water Payable

ACCRUED EXPENSES AND OTHER
LIABILITIES

Taxes – Property & General
State Fuel Taxes
Federal Transportation
Taxes
Royalties Payable
Pension Plan – Hourly
Salaries and Wage Accrual
Vacation Pay Accrual
State Transportation
Taxes

EXHIBIT B