



STATE BOARD OF EQUALIZATION

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January 15, 1993

BURTON W. OLIVER
Executive Director

Ms. R--- N. H---
S---, B---, G---, S--- & M---
XXXX --- ---, Suite XXX
--- ---, CA XXXXX

Re: SY -- XX-XXXXXX

Dear Ms. H---:

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

"A. Introduction

"The facts of the transaction are as follows. T--- Corporation ('T---') is a Virginia corporation with its executive office located in --- ---, California. The principal business of T--- involves the development, sale, leasing and servicing of facsimile and other telecommunications equipment and supplies. T--- conducts business in all 50 states. T--- holds California sales tax permit number SY -- XX-XXXXXX in connection with its business. T--- is a presently a wholly owned subsidiary of A--- - M---, Inc. ('A--- - M---'), a Delaware corporation, which is a wholly-owned subsidiary of A--- G---, Inc. ('A---'), a Delaware corporation. Shares of A---'s Class A Common Stock are traded over the National Market System of the National Association of Securities Dealers, Inc. Automated Quotation System ('NASDAQ/NMS') and are held by more than 2,800 persons. Shares of A---'s Class B Common Stock are held by approximately 13 persons.

"B. The Transaction

"The assets of T--- consist of (a) tangible and intangible property located within and without California used in the course of its facsimile and telecommunications business, and (b) 339,300 shares of Class A common stock of A--- (the 'A--- Shares') and an intercompany receivable due from A--- (the 'A--- Receivable'). T--- proposes to transfer all of its assets other than the A--- Shares and the A--- Receivable, i.e., all of the

tangible and intangible property used in the course of its facsimile and telecommunications business, together with all of its liabilities, to a newly formed subsidiary hereafter referred to as 'Newco', in exchange for first issue stock of Newco. Immediately after the transfer, T--- will own 100% of the issued and outstanding shares of stock of Newco.

"The assets to be transferred by T--- to Newco consist of the following:

- Cash
- Notes, accounts and contracts receivable
- Inventories
- Prepaid expenses
- Buildings and improvements
- Machinery and equipment
- Leasing Equipment (1)
- Leaseholds and improvements
- Motor vehicles
- Stock of subsidiaries
- Deferred income taxes
- Other assets

(1) Leased to customers in the regular course of business.

"The liabilities to be transferred from T--- to Newco consist of the following items:

- Accounts payable, trade
- Accrued liabilities
- Deferred service, deferred interest, deferred rent

"C. The Reorganization After the Transaction

"Immediately after T--- transfers the above-described assets and liabilities to Newco and receives the shares of Newco stock, and pursuant to a plan of reorganization adopted by A--- for valid business purposes, T--- will distribute the shares of Newco to its parent, A--- Mayfair, who will in turn distribute the shares of Newco to its parent, A---, who will then contribute the shares of Newco to a newly-formed subsidiary, T--- Industries, Inc. ('Industries') in exchange for all of the issued and outstanding shares of Industries. As a result, Newco will become a wholly-owned subsidiary of Industries, which in turn will be a wholly-owned subsidiary of A---. A--- will then 'spin-off' and distribute the Class A common shares of Industries to its Class A shareholders (other than T---) on a one-share-for-one-share basis, and

will distribute the Class B Common share of Industries to its Class B shareholders on a one-share-for-one-share basis. As a result of the distribution of the Industries stock to the A--- shareholders, Industries will become independent of A--- and at the date of the distribution will be owned by the shareholders of A--- in the same proportion that they own shares of A---. The principal asset of Industries will be all of the stock of Newco. The above transaction will qualify as a tax-free reorganization and a tax-free spin off under Sections 368(a)(1)(D) and 355, respectively, of the Internal Revenue Code; a ruling to this effect is presently pending with the Internal Revenue Service."

With respect to these transactions you have asked the following questions:

"1. Are we correct in our conclusion that the transfer of assets by T--- to Newco qualifies as an exempt occasional sale pursuant to CRTC Sections 6006.5(b), 6367 and 6281?"

Revenue and Taxation Code section 6367^{1/} exempts from sales and use tax occasional sales of tangible personal property and the storage, use, or other consumption in this state of tangible personal property, the transfer of which to the purchaser is an occasional sale. The exemption does not apply to motor vehicles; however, section 6281 provides an exemption for sales and purchases of motor vehicles which is similar to the exemption which applies to occasional sales defined under section 6006.5(b).

Section 6006.5(b) includes the following definition of an occasional sale:

"(b) 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."

Regulation 1595(b)(2) provides that "substantially all of the property" means 80 percent or more of all the *tangible personal property* held or used in the course of activities, including tangible personal property located outside of this state. Real property and intangible property are not included in the test to determine if there was a transfer of substantially all of the property. See BTLG, Annotations 395.1260 and 395.1500.

^{1/} Unless otherwise noted, all further statutory references are to the Revenue and Taxation Code.

Regulation 1595(b)(2) also provides that the real or ultimate ownership is "substantially similar" to that which existed before a transfer if 80 percent or more of that ownership of the tangible personal property is unchanged after the transfer.

According to your letter, T--- will transfer all of its tangible personal property to Newco. The only property T--- will retain is intangible property. Therefore, the "all or substantially all of the property" requirement is met.

It also appears that the real or ultimate ownership requirement is met. Immediately before and after the transfer, the ultimate owners of the property are the Class A and Class B common stock shareholders of A--- since Newco is a wholly-owned subsidiary of T---, which is a wholly-owned subsidiary of A--- - M---, which is a wholly-owned subsidiary of A---.

The Board, however, will scrutinize a transaction where the shares of a subsidiary are sold or transferred to third parties immediately after the transfer of property to the subsidiary. If there is no business purpose other than the avoidance of sales or use tax for the transfer of assets to a subsidiary and thereafter a transfer of its stock to a third party, the Board will disregard the transaction and will regard the transaction as a sale of tangible personal property from the parent corporation to the third party. Where the stock of a parent corporation is publicly traded, the Board will not disregard a transaction as an occasional sale merely because the real or ultimate ownership changes because of routine public sales and purchases of publicly traded stock.

From the facts you have given us, it appears that even after the several transfers of the stock of Newco, the real or ultimate ownership of the property transferred to Newco will be the Class A and Class B common stock shareholders of A--- and that such shareholders' ownership interests in Newco via Industries will be in the same proportion as their ownership interests in A---. We are assuming that the only changes in ownership interests in A--- immediately before distribution of the Industries stock to its shareholders will be due to routine public trading of its Class A shares. We are also assuming that immediately after the transfer of the Industries stock to the shareholders of A--- there will be no other unusual stock transactions. If these assumptions are correct, the exemptions under sections 6367 and 6281 apply to the transfer of the tangible personal property, including the motor vehicles, to Newco.

"2. Are we correct in our conclusion that the assumption of liabilities by Newco is not taxable consideration provided the sale qualifies as a CRT Section 6006.5(b) occasional sale?"

Assumption of liabilities is consideration and is included in the gross receipts from the sale of tangible personal property. However, since the exemptions under sections 6367 and 6281 appear to apply to the sale of the tangible personal property to Newco, the gross receipts from this sale are exempt from tax.

"3. In the event the CRTC Section 6006.5(b) occasional sale test is not met, would the sale be otherwise exempt pursuant to Sales and Use Tax Regulation 1595(b)(4)?"

No. T--- received consideration in the form of assumption of liabilities by Newco. Since T--- is engaged in the business of selling and leasing tangible personal property and holds a seller's permit, its sale of tangible personal property to Newco does not qualify as an occasional sale under section 6006.5(a). Tax would apply because Regulation 1595(b)(4) provides that tax applies if the transferor receives any consideration other than the first issue of stock, such as an assumption of indebtedness, and the transfer does not otherwise qualify for exemption.

"4. If the answer to question 3 is yes except for the fact that liabilities are being transferred, what liabilities assumed by Newco are subject to tax (i.e., accounts payable, accrued employee benefits, etc.) in determining other consideration pursuant to Regulation 1595(b)(4)?"

If the transfer to Newco is not an occasional sale under section 6006.5(b), the starting point for determining the measure of tax is the total amount of liabilities assumed by Newco, including accounts payable, accrued employee benefits, and indebtedness secured by real property. This amount is multiplied by the ratio of the total value of the tangible personal property located in California to the total value of all property transferred to Newco. For example, if the total amount of liabilities assumed is \$5,000,000 (and no other consideration is given), the total value of the tangible personal property located in California is \$2,000,000, and the total value of all property transferred is \$10,000,000, the measure of tax is \$1,000,000. [\$5,000,000 X (\$2,000,000/\$10,000,000)]

"5. What procedures are necessary to obtain clearances for vehicles transferred pursuant to CRTC Section 6281?"

Newco should call a local Board office and ask for the Compliance Supervisor or Tax Compliance Specialist who handles the BT-111 Forms. These forms are exemption certificates issued by the Board for presentation to the DMV when registering vehicles whose purchases are exempt under section 6281. The supervisor or specialist will be able to explain the procedure for obtaining the form and to list all of the documents which must be presented for each vehicle. Newco should also present a copy of this letter to the local office.

"6. Will any of the transfers of stock among the various entities as part of the reorganization plan described above have any California sales or use tax consequences?"

As discussed under question 1, if the transfers of the Newco stock among the various entities as part of the reorganization plan which you described have an independent business

purpose and are not part of a plan whose sole purpose is to transfer tangible personal property free of tax, the transfer of Newco stock will not affect the sections 6006.5(b) and 6387 exemption or cause the transfer of property to Newco to be taxable.

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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