

**M e m o r a n d u m****295.0747**

To: Audit Review &amp; Refunds

September 9, 1975

From: Thomas L. Hartigan  
Tax Counsel

Subject: SB -- XX XXXXXXX

Your memorandum to the legal department of September 8, 1975 referred to a letter from Attorney R--- E. G---, dated August 28, 1975, and asked whether litiagation referred to by the attorney would have any effect on the sales price of a vessel on which use tax was predicated. We will summarize the litigation and give our opinion later. At this point, however, we refer you to the attached history of this account (and a related account) prepared for us by Charles V. Johnson of the Occasional Sales Unit.

In brief, that history reveals that the seller was a R--- B. W---; the purchaser was E--- P---, as agent for the B--- of the S---, a corporation. Initially, the Board used \$8,000 as the sales price based on an estimate by the Board's staff. Later, in reliance on pleadings by the litigation referred to above, the Board used \$60,000 as the agreed sales price. There have been partial payments as to the tax computed on the initial estimated sales price, and as to the tax computed on the agreed sales price discovered later. Letters by counsel at various times in the interim have been treated as claims for refunds of the amounts paid.

The \$60,000 agreed sales price to be paid by the purchaser, was \$10,000 in cash, assumption of an obligation of seller in the amount of \$25,000, and execution of a promissory note to seller in the amount of \$25,000. The purchaser paid the \$10,000 cash.

Thereafter seller assigned the promissory note to J--- L---, and the litigation began with a complaint filed by L--- against the purchaser for payment of the note. The purchaser answered and cross-complained against L---y and W--- setting forth defenses and seeking various forms of relief based on allegations that seller's representations concerning the vessel were false; but significantly it is noted that the purchaser admitted in the cross-complaint that the agreed sales price was \$60,000.

Attorney G---, representing purchaser, now seeks to reduce the agreed sales price as the measure of tax on the basis of the allegations of fraud set forth in his client's pleadings.

It is our view that once a sales price is agreed upon and a transaction completed based thereon, a dispute thereafter between seller and purchaser as to the price does not have any bearing on the use of the agreed price in computing the use tax. Particularly in point in support of this view is the decision in Southern California Edison Co. v. State Board of Equalization, 7 C 3d 652 (1972).

In that case, Edison sought a partial refund of sales and use taxes paid on purchases of electrical equipment. Although Edison conceded that the taxes were accurately computed with respect to the original agreed-upon sales prices, it contended that the sales price should be reduced because of a later settlement with suppliers of the equipment reducing the amount Edison had to pay the suppliers. The settlement was in lieu of final adjudication of litigation concerning that amount. The court held that the subsequent settlement did not reduce the sales price initially agreed upon, and on which the tax was computed, and no refund was allowed.

The court stated (pp. 661) "An overall view of the sales and use tax statutory scheme, however, indicates that the Legislature intended the 'sales price' and 'gross receipts' terminology of Sections 6011 and 6012" (Revenue and Taxation Code) "to refer to the price agreed upon at the initial sales transaction and not to the net amount which the buyer ultimately pays for the goods purchased." (Emphasis is that of the court.)

Here there is neither a settlement or a judicial determination that the initial sales price was, in fact, fraudulently obtained, that is, the litigation is still in the pleadings stage. Even if subsequently there is a settlement or adjudication reducing the amount owed by the subject taxpayer with regard to the transaction concerning the vessel, it would not have the effect of reducing the initial agreed sales price on which the tax was predicated. Therefore, the petition or petitions for refund should be denied.

TLH:js  
attachment

cc: Occasional Sales Unit (CVJ)