



**STATE BOARD OF EQUALIZATION**

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February 22, 1995

BURTON W. OLIVER  
*Executive Director*

REDACTED TEXT

RE: [No Permit Number]  
X TRANSPORTATION AUTHORITY  
Rail Transit Vehicles

Dear REDACTED TEXT:

Your letter dated November 22, 1994 to Staff Counsel Donald Fillman has been referred to me for a response. I apologize for the lateness of this response. Mr. Fillman transferred to another section, and I did not receive the assignment until last month. You ask the following question:

"Is the X TRANSPORTATION AUTHORITY responsible for payment of sales or use taxes on the acquisition of heavy rail transit vehicles, purchased in 1988 from an Italian manufacturer, to be used in REDACTED TEXT Rail Subway Project ["the Project"]; or in the alternative, would this contract qualify for any form of exemption or relief from the imposition of the payment of sales or use taxes?"

I. FACTUAL BACKGROUND.

You indicate that the former Y TRANSIT DISTRICT, which is now a part of X TRANSPORTATION AUTHORITY, entered into a contract for the purchase of 30 cars with an option to purchase 28 more, for use on the Project. That option is currently being exercised. You further indicate that the contract was executed with the seller, ITALIAN COMPANY, an Italian

company. You quote Section 32 of the contract as follows:

"The contractor is responsible for paying all retail sales, income, real estate, sales and use, transportation, export, import, and special taxes and duties applicable to, and assessable against any materials, equipment, processes and operations incidental to or involved in the procurement. The Contractor is responsible for ascertaining and acquainting itself with such taxes and making all necessary arrangement to pay them. The prices established in the Contract shall include compensation for any taxes the Contractor is required to pay by laws and regulations in effect on the Bid Opening Date."

You indicate in your letter that a copy of the contract itself is attached to the letter, but none was attached to the copy I received.

You state that you have reviewed Revenue and Taxation Code sections 6368.5, 6368.7, and 6369.4, and have concluded that the sale of rail transit vehicles is not exempt from tax. You appear to be primarily concerned about whether or not the X TRANSPORTATION AUTHORITY is required to reimburse ITALIAN COMPANY for the new taxes that were imposed in 1991.

## OPINION

### A. Sales and Use Tax Generally.

In California, except where specifically exempted by statute, Revenue and Taxation Code section 6051 imposes an excise tax, computed as a percentage of gross receipts, upon all retailers for the privilege of selling tangible personal property at retail in this state. (Unless otherwise noted, all statutory references are to the Revenue and Taxation Code.) "[I]t shall be presumed that all gross receipts are subject to tax until the contrary is established. The burden of proving that a sale of tangible personal property is not a sale at retail is upon the person who makes the sale. . ." (§ 6091.) "Exemptions from taxation must be found in the statute." (Market St. Ry. Co. v. Cal. St. Bd. of Equal. (1953) 137 Cal.App.2d 87, 96 [290 P.2d 201].) "The taxpayer has the burden of showing that he clearly comes within the exemption." (Standard Oil Co. v. St. Bd. of Equalization (1974) 39 Cal.App.3d 765, 769 [114 Cal.Rptr. 571].) The retailer owes the sales tax but may collect sales tax reimbursement from the purchaser pursuant to agreement. (Civ. Code § 1656.1.)

### B. Fixed-Price Contracts Generally.

As you are aware, on June 30, 1991, the Legislature enacted Assembly Bill 2181, Statutes 1991, Chapter 85. This bill amended sections 6051 and 6201, and added sections 6051.2, 6051.5,

6201.2, and 6201.5, which raised the statewide sales and use tax rate to seven and one-quarter percent (7 1/4%). This bill also added section 6376.1, which provides that certain contracts executed prior to July 15, 1991, in which the seller is obligated to sell or the buyer is obligated to purchase tangible personal property for a fixed price, are not subject to the new rates. Subsequently, the Legislature enacted Senate Bill 180, Statutes 1991, Chapter 236, which amended section 6376.1 to provide that construction contracts entered into prior to July 15, 1991, qualify for the exemption, and that the exemption does not apply to contracts for any period of time in which one party to the agreement has the right to terminate the agreement upon notice, whether or not the right is exercised.

In determining whether a contract is a "fixed-price" contract, we have consistently required that it satisfy the following criteria: (1) it be executed binding prior to the date the tax increase became effective; (2) neither party has a right to terminate the contract conditioned solely upon notice; (3) the agreement must fix the amount of all costs at the outset; and (4) the agreement must include a provision which fixes the tax obligation on a tax-included basis or sets forth either the amount or the rate of tax and does not provide for an increase in the amount of tax.

#### C. Tax Consequences to X TRANSPORTATION AUTHORITY.

In addition to the state tax increases recited above, operative April 1, 1991, the Los Angeles County Transportation Commission imposed a 0.5% transactions and use tax. A "grandfather clause" for fixed-price contracts was enacted for the statewide tax increase (§ 6376.1), and fixed-price contracts are exempted from after-imposed district taxes. (§§ 7261(g) & 7262(f).) Does this contract qualify?

We are of the opinion that it does not. You indicate that these cars will be purchased under an option which is currently being negotiated. An "option" is a contract, supported by its own consideration, to keep an offer to sell open. Where there is consideration, the option is irrevocable. The purchase is thus not completed until after the option is exercised. We have previously determined that any modification to the original purchase contract which requires its own separate consideration, like a change order to a construction contract, is a new contract which is not entitled to grandfather protection. The parties will take the new tax rates into account when negotiating sales price. As a result, since the agreement to purchase these new rail cars will be executed well after the higher rates have taken effect, it fails the first criterion listed above and so will not qualify for exemption from the higher state rates and the new district tax as being for a fixed price.

REDACTED TEXT

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February 22, 1995  
800.0014

I hope the above discussion has answered your question. If you need anything further, please do not hesitate to write again.

Sincerely,

John L. Waid  
Tax Counsel

JLW:sr