OFFICE OF THE ATTORNEY GENERAL
State of California

150.0060

THOMAS C. LYNCH
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OPINION

of

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No. 67/218

September 6, 1968

THE HONORABLE HERBERT F. FREEMAN, EXECUTIVE SECRETARY OF THE STATE BOARD OF EQUALIZATION, has requested an opinion on the following question:

Does the California Sales and Use Tax Law apply to the sale by --- --- --- --- --- --- --- of a building under an auction contract of sale under which the buyer agrees to remove the house or building from its original location to a place designated by the buyer?

The conclusion is:

The replacement of repealed section 1796 of the Civil Code by section 2107 of the Commercial Code has effectively modified the former statutory rule classifying as personal property all structures that by contract of sale were to be removed or severed from the land on which they stood. As a result of this modification, sales of structures to be removed or severed by the buyer are now classified as sales of real property. Since the sales in the factual situation presented are of this sort, they must be classified as sales of real property. Therefore, the sales and use tax law cannot apply, as that law deals only with the sales of tangible personal property.

ANALYSIS

It is the practice of the --- --- --- --- --- --- --- (hereafter referred to as ---) to hold auction sales of certain buildings condemned in the path of its construction work. As part of the contract of sale, the successful bidder agrees to remove his buildings from the land within a specified time. No removal is allowed, however, until after the buyer has furnished an adequate performance bond, paid the full purchase price and received a written bill of sale from ---. Thus, at the time these sales occur, the buildings are affixed to the land though subject to the later right of removal by the buyers.

This factual situation is, for all relevant purposes, identical to that described in Ops.Cal.Atty.Gen. N.S. 4261 (9142). The question raised in that opinion and reconsidered in Ops.Cal.Atty.Gen. N.S. 4261A (1942) is also identical to that posed here. The decision reached in the former opinion and affirmed in the latter was that such sales of buildings by condemnor government agencies were taxable under the California Sales and Use Tax Law as sales of tangible personal property.

Since these opinions have never been overruled, they would control the answer in this situation if the authorities on which they relied had remained unchanged during the intervening years. It appears, however, that changes in those authorities have occurred that are sufficient to compel a different result.

The earlier opinions, recognizing the sales and use tax statute's lack of helpful definitions, made use of general law sources of property classification. The principal statute relied upon was Civil Code section 658. That section reads as follows:

> "§ 658. [Definition of real property: Severance by agreement.] Real or immovable property consists of:
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> "1. Land;
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> "2. That which is affixed to land;
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> "3. That which is incidental or appurtenant to land;
>
> "4. That which is immovable by law; except that for the purposes of sale, emblements, industrial growing crops and things attached to or forming part of the land, which are agreed to be severed before sale or under the contract of sale, shall be treated as goods and be governed by the provisions of the title of this code regulating the sales of goods."

As may be seen, the language of subdivision (4) quite clearly supported the conclusion that the structures were personal property.

It now must be observed, however, that at the time the earlier opinions were written the reference in subdivision (4) to "the title of this code regulating the sale of goods" led one to those sections of the Civil Code containing the California version of the Uniform Sales Act. This was found in division 3, part 4, title 1 of the Civil Code (sections 1721 -1800). This intra-code reference stemmed from the fact that subdivision (4) had been added to section 658 as part of the same legislative effort that had enacted the Uniform Sales Act. Stats. 1931, ch. 1070, pp. 2234, 2259. Subdivision (4) was further tied to the sales act in that its definition of "goods" was lifted verbatim from that used in Civil Code section 1796, the definitional section of the Sales Act.

It is thus apparent that the 1931 Legislature took pains to carve out from the definition of real property found in Civil Code section 658 the special personal property category found in the new Sales Act. From this it is reasonable to conclude that the definition of "goods" in section 658 was not intended to serve any independent purpose. Rather it was established simply to avoid statutory conflict with what would predictably become a more functional and frequently relied upon definition in the new Sales Act. This conclusion is evidenced by the specific language of subdivision (4) declaring that things to be severed from the land were to be governed by the Sales Act sections of the Civil Code.

On January 1, 1965, however, this symmetry of definition between general law and the personal property sales law came to an end. As of that date the Uniform Sales Act provisions, including the definitions in Civil Code section 1796, were repealed and replaced by the California version of the Uniform Commercial Code. Stats. 1963, ch. 819, p. 1849. The definition of "goods" in Civil Code section 1796 received an effective substitute in the more detailed language of Commercial Code sections 5105 and 2107. The latter section is specifically relevant to the question here and reads as follows:

> "§ 2107. Goods to Be Severed From Realty; Recording. (1) A contract for the sale of minerals or the like or a structure or its materials to be removed from realty is a contract for the sale of goods within this division if they are to be severed by the seller but until severance a purported present sale thereof which is not effective as a transfer of an interest in land is effective only as a contract to sell.
>
> "(2) A contract for the sale apart from the land of growing crops or other things attached to realty and capable of severance without material harm thereto but not described in subdivision (1) or of timber to be cut is a contract for the sale of goods within this division whether the subject matter is to be severed by the buyer or by the seller even though it forms part of the realty at the time of contracting, and the parties can by identification effect a present sale before severance.
>
> "(3) The provisions of this section are subject to any third party rights provided by the law relating to realty records, and the contract for sale may be executed and recorded as a document transferring an interest in land and shall then constitute notice to third parties of the buyer's rights under the contract for sale." (Italics added.)

As can be seen, section 2107 now classifies as sales of personal property only those sales of structures to be severed from the land by the seller. A sale of a structure to be severed by the buyer is excluded from that sections' definition of a sale of goods. As a result of this exclusion from the Commercial Code, a sale of the latter type must be classified and treated by the parties as one of realty. The previously mentioned statutory dissymmetry arises from the fact that the Legislature did not change Civil Code section 658(4). That section, in conflict with section 2107, retains the classification as goods of any structure to be severed from the land by either party.

The failure to conform section 658(4) to the Commercial Code appears to have been a legislative oversight. See, 51 Ops.Cal.Atty.Gen. 113, 115 (1968); 43 Ops.Cal.Atty.Gen 148, 150 (1964). This is indicated by that section's retention of the language referring to the sale of goods as being covered by the provisions of the Civil Code. This, of course, is totally inaccurate as the Commercial Code is entirely separate from the Civil Code. It seems logical that if the Legislature had consciously wished to retain for some purpose the old Sales Act definition in section 658 (4) it would have at least amended the final clause to refer to the proper code. This failure to tidy up section 658 (4) indicates that the Legislature did not consider that section in the massive effort put forth in enacting the Commercial Code.

It is our conclusion that this conflict between Commercial Code section 2107 and Civil Code section 658 (4) should be resolved by favoring the definition in the former. It is our further conclusion that this decision compels the classification of the sales at issue herein as sales of realty not subject to the sales and use tax law.

The reasons for this are several. On the first point, it must be remembered that section 658 (4) was originally enacted simply to maintain definitional conformity with the personal property sales act of the time. It is therefore reasonable to assume that had the 1963 Legislature considered the conflict described herein, it would have acted to conform that section to the new personal property sales act. Because of this, there seems to be no bona fide argument in favor of preferring section 658 (4) over section 2107. Certainly commercial transactions will not be influenced by nor cast upon the basis of the former. The latter, on the other hand, will control the nature of innumerable such transactions. Therefore, to the extent that a resolution of the conflict between the two is required, the proper course is clearly to favor the more significant definition of section 2107.

As to the applicability of that section to the sales and use tax, it must be again noted that the sale and use tax provisions of the Revenue and Taxation Code contain nothing that is helpful in classifying a particular item of property as real or personal. In light of this it seems reasonable to rely for definitions upon the commercial laws under which retailers subject to the sales and use tax must operate. These laws, and the Commercial Code in particular, are intended to conform to commercial realities. It thus does not seem improper for the tax authorities to rely on them for definitional aid in cases where the tax statutes are of no assistance. This approach has the desirable aspect of having the tax consequences of a transaction reflect the neutral commercial realities of that transaction. Apart from legislative assistance in this definitional problem, the only alternative would be resort to some sort of unpredictable and unsatisfactory ad hoc definitional process.

Finally, it should be noted that this opinion does not alter the conclusion reached in 2 Ops.Cal.Atty.Gen. 149 (1943). That opinion dealt with a situation where the seller of structures affixed to land was to perform the act of removal. Therefore, while the reasoning of that opinion might be modified by the subsequent legislative changes discussed herein, the conclusion that such sales are taxable remains unaltered by this opinion.

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M e m o r a n d u m

150.0060

To: San Francisco – Auditing (LC:REP) Date: Sept. 12, 1968

From: Tax Counsel (TPP)

Subject:

In your letter of February 6, 1967, addressed to Headquarters – Principal Auditor, you inquire concerning the application of sales tax to sales of buildings by --- --- --- --- --- --- ---.

In answer to your inquiry, we are enclosing a copy of an opinion which we have recently received from the Attorney General.

TPP:smk [lb]