

M e m o r a n d u m**325.0089**

To: Mr. Robert Nunes

Date: April 12, 1971

From: Gary J. Jugum

Subject: Platinum Catalyst

This is in response to your memorandum of March 3, 1971, to Mr. T. P. Putnam by which you forwarded to us a number of questions concerning the application of the principles set forth in your letter of November 5, 1970, to Mr. D--- B. S---, Chairman, Excise Tax Committee, W---.

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I. Responses to your memorandum of January 19, 1971:

Los Angeles (Transmittal of February 15, 1971)

[1] “[S] Co. has not reported any use tax on purchases of new platinum metal since September 30, 1964. [S]’s contention is that the platinum used in California comes from a “commingled” mass of platinum maintained at [U] O--- Company [U]. The “commingled” mass consists of both new and used platinum recovered from spent catalyst returned by their several refineries in this country. [S]’s theory is that so long as the quantity of used or recovered platinum on hand at [U] exceeds their California requirement at the time a California refinery draws from the “commingled” mass, no California tax is due.” [Memorandum from J. K. G--- to Mr. S. S. T---, February 5, 1971.]

See our memorandum of April 7, 1971, to Mr. Donald F. Brady, re “Platinum Catalyst – S--- O--- Corporate Pool/[SO]” where we take the position that where a commingled mass of fungible goods, part “California tax paid” and part “ex California tax,” is maintained by a taxpayer outside this state, taxpayer may bring into this state, for use here, without payment of additional California tax, an amount of the goods equivalent to the amount of California tax-paid goods maintained in the commingled mass at the time withdrawal is made--a “tax-paid-first-out” principle with respect to withdrawals made by taxpayer for use in this state. We think that this position is consistent with the principle of sections 6245 and 6095 of the Revenue and Taxation Code. Additionally, by virtue of the fact that California tax has been paid on a part of the commingled mass of goods, that part has already been identified as having been purchased by taxpayer for use in this state.

[P] Co. –

- [2] “[P] would order, and [U] would ship, fresh catalyst, including the platinum and rhenium activator, the catalyst would be leased at the regular monthly rate specified by contract. The platinum and rhenium activator would be leased at their respective “turnaround” charges (flat dollar amounts per troy ounce for 35 days).

“Upon receipt of the fresh catalyst, [P] would ship to [U] the spent catalyst from its reactors. [U] would recover the rhenium from the spent catalyst and, to the extent of the amount recovered, terminate the lease of the rhenium contained in the fresh catalyst. Title to the recovered rhenium would transfer to [U]. Title to the rhenium content of the fresh catalyst would transfer to [P]. Since [P] now leases all its platinum requirements from [U], ... no transfer of title to platinum would occur.

“Would the measure of tax include the value of the rhenium component of the spent catalyst subsequently recovered by and furnished to the catalyst manufacturer by the refiner?” [Memorandum from G--- S--- to Mr. G--- G---, February 8, 1971.]

The measure of tax would include the value of the rhenium component of the spent catalyst subsequently recovered by and furnished to the catalyst manufacturer by the refiner, as described in example (3) of Mr. Nunes’ letter of November 5, 1970.

San Francisco (Transmittal of February 1, 1971)

SO –

- [3] “What is the measure of tax when noble metal is exchanged? Cost? Producer’s price? Market price?”

“Sales price,” the measure of tax, includes “the total amount for which tangible personal property is sold... valued in money, whether paid in money or otherwise....” The agreements with which we are familiar provide that. “... should REFINER’S platinum stock account deficit exist ninety days after (shipment of the fresh catalyst) REFINER hereby authorizes [U] to purchase for the account of REFINER a quantity of platinum equal to REFINER’S platinum stock account deficit at the then market price of the platinum so required.” When the refiner makes up the deficit amount owed to [U], the measure is not cost but the then current market value of the platinum furnished by the refiner. Information supplemental to the contract may indicate that as between [U] and the refiner “market price” means “producers’ price.”

- [4] “Under fungible goods sections 6095 and 6245, how should a transfer from one mass of commingled goods to another separate mass of commingled goods be handled?”

The example given indicates a transfer from SO to A--- C--- of platinum maintained by SO, in its corporate pool, at [U] The transfer to A--- C--- should be treated in the same manner as transfers from SO to its corporate subsidiaries, as described in our memorandum of April 7, 1971, to Mr. Brady. Additionally, we think that where a commingled mass of fungible goods, part California tax paid and part ex California tax, is maintained by a taxpayer outside this state, taxpayer may transfer, to third parties, from that mass, amounts of the goods up to the amount of the ex California tax portion of the mass, without loss of the California tax-paid status of the remaining portion of the commingled mass of fungible goods--an “ex California tax first out principle” with respect to sales to third parties.

- [5] “How should we include the out-of-state salvage charges in the measure of tax when the salvage charge may have been paid by SO or by one of the out-of-state subsidiaries of SO? Also, how should we include the salvage charge in the measure of tax when the subsequent batch of catalyst may or may not come into California?”

Only those salvage charges connected with catalyst shipped into California are taxable. That is, with respect to each “load” of fresh catalyst shipped into this state the salvage charge made with respect to that “load” is subject to tax. Tax applies when the platinum is returned to California.

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II. Questions previously raised:

San Francisco (Memoranda of November 23, 1970, and January 11, 1971)

- [6] “How is the value ‘... of the platinum component of the spent catalyst subsequently furnished to the catalyst manufacturer...’ [as described in Mr. Nunes’ letter of November 5, 1970] to be determined? Cost? Market price? Producer's price?”

See answer to question [3] above.

[7] “How many ounces are subject to use tax” in the following example:

“Refiner’s Platinum Account at the O/S Catalyst <u>Manufacturer’s Plant</u> ”	
“1-10-70 (3) 3000 oz	1-1-70 (1) 2000 oz 1-5-70 (2) 2000 oz.

- “(1) Salvaged from refiner’s spent catalyst that came from refiner’s out of state refinery wherein the catalyst had been used for two years.
- “(2) New platinum purchased by refiner ex tax from O/S supplier.
- “(3) Platinum content of fresh catalyst shipped to refiner in California.

“Question: How many oz are subject to use tax?”

One thousand five hundred ounces are subject to tax. The refiner should be regarded as having made a pro rata withdrawal from the commingled inventory. [CF. Union Oil Co. v. Johnson, 58 Cal.App.2d 636.]

[8] “How many ounces are subject to use tax” in the following example:

“Refiner’s Platinum Account at the O/S Catalyst <u>Manufacturer’s Plant</u> ”	
“1-10-70 (3) 2000 oz	1-1-70 (1) 2000 oz 1-5-70 (2) 2000 oz.

- “(1) Salvaged from refiner’s spent catalyst that came from refiner’s California refinery wherein the platinum content had been California tax paid.
- “(2) New platinum purchased by refiner O/S ex tax and shipped to catalyst manufacturer.

“(3) Platinum content of fresh catalyst shipped to refiner’s California refinery.

“Question: How many oz are subject to use tax?”

Zero ounces are subject to tax. See discussion in [1] above.

[9] “If a refiner uses fresh platinum catalyst at one of its out-of-state refineries for six months and then ships this catalyst to a California refinery where it will be used for two years more, is the catalyst and platinum content subject to use tax assuming that it was the refiner’s intention to follow this procedure when he first purchased the catalyst?”

No.

[10] “If a refiner uses fresh platinum catalyst (use tax acquisition) at one of its California refineries for six months and then ships this catalyst to an out-of-state refinery where it will be used for two years more, is the catalyst and platinum content subject to use tax assuming that it was the refiner’s intention to follow this procedure when he first purchased the catalyst?”

Yes.

[11] “In example (3) [of Mr. Nunes’ letter of November 23, 1970] are we interpreting the application of tax correctly to mean that when a California refiner exchanges its California tax-paid platinum with an out-of-state subsidiary refiner...that the transaction should be treated as a purchase of new ex-tax platinum from the subsidiary? ... If the transaction should be treated as a purchase of new ex-tax platinum from the subsidiary, then it appears that sections 6095 and 6245 pertaining to fungible goods may be included.

In our opinion the transaction should be treated as a purchase of new ex-tax platinum. The principle of commingled fungible goods, discussed in [1] above, would then be relevant, as indicated in the following examples:

“Refiner’s Platinum Account
at the O/S Catalyst
Manufacturer’s Plant

	1-1-70 (1) 2000 oz
	1-5-70 (2) 2000 oz.
“1-10-70 (3) 2000 oz	
“1-15-70 (4) 2000 oz	

- “(1) Salvaged from refiner’s spent catalyst that came from refiner’s California refinery wherein the platinum content had been California tax paid.
- “(2) Salvaged from subsidiary’s O/S refinery and purchased by SO via exchange.
- “(3) Platinum content sold to O/S subsidiary via exchange as described in our reports of 4-7-69 and 7-1-69.
- “(4) Platinum content of fresh catalyst shipped to refiner in California for own use.”

Tax does not apply to platinum shipped to refiner in California for own use. This is the “ex California tax first out” principle with respect to property withdrawn for sale outside this state.

“Refiner’s Platinum Account
at the O/S Catalyst
Manufacturer’s Plant

	1-1-70 (1) 2000 oz
	1-5-70 (2) 2000 oz.
“1-10-70 (3) 2000 oz	
“1-15-70 (4) 2000 oz	

- “(1) Salvaged from refiner’s spent catalyst that came from refiner’s California refinery wherein the platinum content had been California tax paid.
- “(2) Salvaged from subsidiary’s O/S refinery and purchased by SO via exchange.

“(3) Platinum content of fresh catalyst shipped to refiner in California for own use.

“(4) Platinum content sold to O/S subsidiary via exchange.

Tax does not apply to platinum shipped to California. This is the “tax paid first out” principle, with respect to withdrawals for use by taxpayer in this state.

Los Angeles (Transmittal of November 18, 1970)

[12] “In example 4 [of Mr. Nunes’ letter of November 5, 1970], title to the ‘spent’ platinum is retained by the refiner. Presumably the refiner would pay the manufacturer in full for the ‘load.’ Does this occur? It would seem unusual to tie up large amounts of capital in this manner.” [Memorandum from J--- T. Q--- to Mr. J--- W. T---, November 17, 1970.]

This kind of transaction probably does not occur very often, but the example was added to make our explanation of our position analytically complete.

[13] “[In example 5 of Mr. Nunes’ letter of November 5, 1970] there is a probability that occasionally new platinum is obtained by refiners from original sources. Our audit contains information that [S] obtains platinum directly from the producers. In such a case, how do we get tax?” [Ibid.]

Tax applies upon the shipment of the ex tax platinum into this state for use here. See also discussion in respect to questions [1] and [8] above.

[14] “I am not in accord with the facts and application of tax” [as outlined in example (3) of Mr. Nunes’ letter of November 5, 1970].

“This example requires clarification. Mr. Nunes in his description of the problem and the application of the tax refers to the rental of platinum catalyst and the rental of the platinum component of the catalyst as if these were interchangeable terms. This is not correct.

“Mr. Nunes also appears to imply that the catalyst manufacturer uses a ‘platinum account’ to account, by weight, for the precious metal receipts and issues only under special circumstances. It is my understanding that it is a regular business practice for these companies to maintain memorandum accounts of this nature for the oil refiners.

"It has been our experience in this office that the only rental encountered in audits of oil companies involving this problem has been the rental of the platinum component or the catalyst.

.....

"It is my understanding that, even when a rental or the platinum component is involved, the manufacturer issues a regular billing for the platinum catalyst with title passing upon shipment. Under these terms the transaction is subject to the use tax.

"Since the platinum supplied by the manufacturer becomes an integral component of a finished product (platinum catalyst) upon which title passes at the shipping point, it appears to be inconsistent to accept passage of title to the platinum component at any other point.

"Also, it appears from the actions of the parties involved that a sale of the platinum component is contemplated from the inception of the transaction. The language used in the contract is misleading and not in accord with the factual situation."

With respect to the question as to whether the rental of an integral component (platinum) of a finished product (platinum catalyst) is permissible under the Sales and Use Tax Law, we see no reason why such an arrangement should not be recognized in this case. According to the basic Catalyst Supply Contract of [U] with which we are familiar, "Title to catalyst, except title to platinum (in catalyst), leased by [U] to REFINER, if any, ... shall pass to refiner upon delivery of such catalyst by [U] to the carrier at [U]'s point of shipment." The contract further provides that, "Title to the used catalyst, exclusive of the platinum content thereof, shall pass to [U] upon delivery of such catalyst by refiner to the carrier at refiner's point of shipment."

In our opinion tax applies to the "recovery charge" and the contract "price of catalyst" (but does not include the value of the refiner-furnished platinum component) at the time the catalyst is brought into this state. The use tax is applicable with respect to these charges. Tax then applies, upon the subsequent passage of title to the platinum component of the catalyst, in the manner described in example (3) of Mr. Nunes' letter. This tax is a sales tax.

This case just considered differs factually from example (3) given in Mr. Nunes' letter in that this case involves both a sale of tangible personal property under section 6006(a) of the Revenue and Taxation Code and a fabrication of consumer-furnished property under section 6006(b) of the code whereas the example given in Mr. Nunes' letter involves exclusively a "fabrication" transaction under section 6006(b).

Mr. Nunes' letter of November 5, 1970, was intended, as suggested above, to be analytically complete. We recognize that it is a regular business practice for these companies to maintain memorandum accounts for platinum and other precious metals.

Regulation 1641 "Credit Sales and Repossessions" provides that:

"If tangible personal property is, for all intents and purposes, sold, but the transaction is designated as a lease or rental for the purpose of retaining title in the seller as security for payment of the purchase price, or for the purpose of avoiding the tax, the transaction is taxable [at its inception] as a sale under a security agreement."

Where, however, a transaction is structured by the parties in such a way as to bring it within the purview of the Sales and Use Tax Law, and where the agreement, if given effect as structured does not lead to tax avoidance, we have recognized the agreement as effective on its own terms. [See Standard Oil Co. v. State Board of Equalization, 232 Cal.App.2d 91.]

In our opinion we should regard these transactions as true lease transactions. The parties will avoid no tax by paying tax on both the rental payments and the subsequent sale of the leased platinum to the refiner.

[15] "I am not in accord with the facts" [as described in example (4) of Mr. Nunes' letter of November 5, 1970.]

"In order to maintain a proper balance in this account it would be necessary for the manufacturer to charge the account for the quantity of platinum shipped and credit the account for the quantity of platinum recovered from the spent catalyst returned."

We agree. However, this example is intended to illustrate the application of the tax where taxpayer pays tax on two "loads" of platinum and then continues to maintain a credit balance with the catalyst manufacturer. Subsequent transactions would then be taxed on the "net exchange" basis and not on the "trade-in" basis.

GJJ/ab

Gary Jugum