

**STATE BOARD OF EQUALIZATION**

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June 16, 1995

BURTON W. OLIVER
Executive Director

Mr. K--- R. N---
Corporate Counsel
A--- B--- L---, Inc.
XXXX - XXth ---- ---
I--- P---
---, MN XXXXX

Re: A--- B--- L---, Inc.
SR -- XX-XXXXXX

Dear Mr. N---:

This is in response to your letter dated March 17, 1995 regarding the application of tax to the sale and use of mobile transportation equipment.

You purchased two motor coaches outside of California, and you lease them to W--- C--- T---. Under the lease for each motor coach, W--- is to pay you \$3,575.00 per month for a term of eighty-four months, and has an option to purchase the motor coach for \$67,813.00 at the expiration of the lease. You state that you collect use tax on the rental receipts and remit the tax to the Board. You have attached information about the use of the two motor coaches, and you ask whether the use comes within the exemption for interstate use of mobile transportation equipment (MTE). You also ask what documentation you need to provide to us in order for the transactions to be declared exempt.

Initially, I note that some agreements characterized by the parties as leases are actually sales. However, in the present case, since the lease agreement does not provide for W--- to obtain title at the end of the lease term upon making the required payments, and since the option price is not nominal, the agreement represents a true lease, not a sale at inception. (See Reg. 1660(a)(2)(A).)

Motor coaches, or buses, are included in the definition of MTE (Rev. & Tax. Code § 6023) and the rules applicable to leases of MTE therefore apply. A lease of MTE is excluded from the definition of "sale" and "purchase" for purposes of the Sales and Use Tax Law. (Rev. & Tax. Code §§ 6006(g)(4), 6010(e)(4).) This means that the retail sales are the sales of the buses to you, and you are the consumer of the MTE you lease. Since the sales to you took place outside of California, sales tax does not apply. (Reg. 1620(a)(1).) However, if you are regarded as having purchased the MTE for use in California, that use is subject to use tax unless exempt.

When MTE is purchased outside California for use by leasing in California and the use is not exempt, use tax applies to the purchase price of the MTE unless the lessor makes a timely election to report its use tax liability measured by the fair rental value of the MTE. (Rev. & Tax. Code § 6244(d).) An election to pay tax measured by fair rental value is made by the lessor's reporting and paying tax on that basis with its timely return for the period in which the MTE is first leased. (Reg. 1661(b)(2).) Such an election cannot be revoked, and the lessor must thereafter pay use tax on fair rental value whether the MTE is inside or outside California. When the lessor fails to make a timely election to pay tax on fair rental value, tax is due measured by the purchase price.

Since you indicate that you are already reporting tax on rental receipts and you ask only about the interstate commerce exemption, I assume that you did purchase the MTE for use in California. Thus, unless the use of the MTE satisfies the requirements of the interstate commerce exemption, you must continue to report tax on fair rental value whether the MTE is inside or outside California.

The interstate commerce exemption applies only when the MTE is first functionally used outside California, enters California in interstate commerce, and is used continuously thereafter in interstate commerce, both within and without the state. As stated in Regulation 1620(b)(2)(B): "Use tax does not apply to property purchased for use and used in interstate or foreign commerce prior to its entry into this state, and thereafter used continuously in interstate or foreign commerce both within and without California and not exclusively in California." We use a six-month test period after the MTE's first entry into California to ascertain whether the California use qualifies for the interstate commerce exemption. (Business Taxes Law Guide Annotation 570.0430 (1/7/74, 3/23/84, 1/28/91).)

Since documentation you provided to us indicates that each bus was used in California for intrastate purposes and not exclusively and continuously in interstate commerce during the six months following its first entry into this state, the interstate commerce exemption does not apply to the use of either bus. Therefore, the use of each bus in this state is subject to tax, and as discussed above, you must continue to report and pay tax on fair rental value whether the buses are inside or outside California.

Mr. K--- R. N---

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June 16, 1995
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If you have further questions, please feel free to write again.

Sincerely,

Kelly W. Ching
Staff Counsel

KWC:cl

cc: -- District Administrator