

## STATE OF CALIFORNIA

## BOARD OF EQUALIZATION

## BUSINESS TAXES APPEALS REVIEW SECTION

In the Matter of the Petition for	)	
Redetermination Under the Sales	)	DECISION AND RECOMMENDATION
and Use Tax Law of:	)	
	)	
	)	REDACTED TEXT
REDACTED TEXT	)	

The Appeals conference in the above-referenced matter was held by Staff Counsel Donald L. Fillman on January 23, 1995 in Sacramento, California.

Appearing for Petitioner: REDACTED TEXT

Appearing for the Sales and Use  
Tax Department: REDACTED TEXT

Type of business: Manufacturer and retailer of disposable temperature recorders.

Protested Items

The protested tax liability for the period 10/01/91 through 06/30/93 is measured by:

	<u>Item</u>	<u>State, Local and County</u>
A.	Exempt sales disallowed (actual basis)	REDACTED TEXT
B.	Tax paid purchases resold (not claimed)	REDACTED TEXT
	TOTAL	REDACTED TEXT

Contentions of Petitioner

1. Even if the sales were of tangible personal property, they would be tax exempt under an "agricultural exemption".

2. Petitioner provides temperature recording services, which are tax exempt, rather than sales of tangible personal property, which would be subject to sales or use taxes.

3. Petitioner's competitors are not required to treat their sales as taxable sales of tangible personal property.

4. Petitioner received incorrect advice from the Modesto office of the Board, which directly caused petitioner to not collect sales tax reimbursement on the sale of temperature recording devices.

### Summary of Petition

Petitioner manufactures temperature recording devices which are used for the purpose of permanently recording temperatures over a period of time. The temperature record is made on a paper graph, somewhat like those used to record wind speed or a patient's heart beat.

The typical purchaser is a common carrier which operates refrigerated vans for the shipment of perishable, often agricultural, products. The shipping contract will require that temperatures shall be maintained within an approved range throughout the period of shipment. Petitioner's sealed temperature recording devices are acquired for placement within the van to permanently record the temperatures which occur. The permanently recorded chart may be removed and read by any interested party at the conclusion of the shipment.

In cases where the accuracy of the recorders is disputed, as in the rare case where some spoilage occurs, the temperature recording devices may be returned to petitioner for "calibration clarification". Less than 1% of the devices are so returned. Unless so returned, petitioner's role ends at the time of sale.

Although the devices are primarily sold for a one-time use, petitioner will sell the devices at a reduced price if a customer will agree to return the device for "recycling" after the device has been opened by the customer and the temperature chart has been removed. If the returned device is in good condition it will be provided with a new chart and serial number, and sold again. About 25% are so returned.

Petitioner entered the business in 1991. It contacted the Board's Modesto office to apply for a seller's permit, but was told that the providing of temperature recording services was not a taxable event, and no permit or the filing of sales and use tax returns was required. Petitioner requested written confirmation from the Modesto office by letter of June 22, 1992. The Modesto office requested additional information which was supplied by petitioner by letter of September 9, 1992. Both of petitioner's letters were transferred to Board headquarters in Sacramento on September 24, 1992 for reply.

An initial reply was made by the Principal Tax Auditor by letter of December 7, 1992, which declined to give a positive opinion for lack of information, but which discussed in some detail the difference between (1) a taxable sale of tangible personal property, and (2) the transfer of tangible personal property which is only incidental to the performance of a service, where the service is the true object of the contract.

Once petitioner provided the additional information, a letter to petitioner dated March 17, 1993 concluded that petitioner was selling tangible personal property which was subject to tax. The key to the conclusion was the fact that petitioner's recorders do not have to come back to

petitioner for reading as do other types of recorders. Petitioner is not required to provide any services in order for the recorders to be used by petitioner's customers.

Petitioner acknowledged that the new technology used in its recorders was different than what the industry had been using, and was different than what some of the petitioner's competitors were still providing. Petitioner expressed concern that all taxpayers be treated the same or there would be a competitive advantage to those not required to collect sales tax reimbursement.

Petitioner's customers objected to being charged, for the first time, for sales tax reimbursement, claiming that they should be exempt because they are shipping agricultural products.

### Analysis and Conclusions

1. There never has been an "agricultural exemption". Perhaps petitioner's customers were thinking of a "food exemption". But a temperature recorder is not a food, and no exemption is available based on the product that is shipped. The recorders are consumed by the party that uses them to record the temperatures.

2. Sales and Use Tax Regulation 1501 provides that:

"The basic distinction in determining whether a particular transaction involves a sale of tangible personal property or the transfer of tangible personal property incidental to the performance of a service is one of the true object of the contract; that is, is the real object sought by the buyer the service per se or the property produced by the service."

In the large majority of transactions by petitioner (approximately 99%), no services are rendered by petitioner whatsoever. The recorder is sold to the purchaser and that ends the transaction. If there is no dispute over the accuracy of the recorder, nothing is required of petitioner after the sale. Even if the right to the calibration service is included in the sales price of the recorder, it is clearly not the true object of the sale. The calibration service is rarely needed or used.

The most significant factor in this case is the change in technology involved in verifying temperatures. Prior to the type of system provided by petitioner, temperature verification was accomplished by a different method. A shipper would contract with a party like petitioner to have a sealed recorder placed in the van for the duration of the trip. The recorder had to be returned to the provider for it to be opened that the temperature chart read.

The new technology allows a purchaser to make full use of the recorder without needing the services of the provider. In such cases, there is a fundamental change in the nature of the transaction. It becomes a simple sale of tangible personal property and subject to the sales and use taxes.

Although the historical "service" type of transaction would have been interpreted as being a taxable "rental" of the recorder, the Board has treated these earlier transactions as

primarily a sale of temperature verification services. This explains the initial advice to petitioner from the Modesto office, which was not aware of the change in technology.

Petitioner has expressed two concerns that are shared by the Board: (1) all taxpayers that are engaged in the same type of transaction should be treated the same for tax purposes, and (2) taxpayers should be getting reliable advice from Board employees.

3. Petitioner is not being treated any differently than any other taxpayer under the same facts. If any of petitioner's competitors market the same type of recorders, and sell them on the same terms as those sold by petitioner, their transactions will also be subject to tax.

4. Revenue and Taxation Code section 6596 defines the terms under which a person's failure to make a timely return or payment may be excused. It provides that the Board must find that a taxpayer reasonably relied on written advice from the Board, which was in response to a written request from the taxpayer, if the request fully describes the specific facts and circumstances of the transaction.

The present case is a good example of why section 6596 is in existence. An oral discussion is highly susceptible to being incomplete and misunderstood by either or both of the parties. Petitioner properly followed up its oral discussions with the Board by submitting a written request for a written response. This resulted in the Board learning about the new technology and tailoring its response to the specific facts and circumstances of petitioner's new type of transaction. Although the time which elapsed was longer than either of the parties would have preferred, the issue was resolved perhaps years before an audit would have discovered the error.

#### Recommendation

It is recommended that the tax be redetermined without adjustment.

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Donald L. Fillman, Staff Counsel

April 3, 1995  
Date