

**M e m o r a n d u m****535.0073.090**

To: Petition Unit

March 16, 1990

From: Gary J. Jugum

Subject: R---, Inc.  
Account No. SN OH XX-XXXXXX-010

The petition for reconsideration of successor liability of R---, Inc., was scheduled to be heard by the Board in Torrance on February 21, 1990. The matter was postponed and has been rescheduled for the week of May 20, 1990.

The staff is prepared to recommend to the Board that the tax be reduced.

A--- and C---, Inc., was primarily engaged in a trucking business. On December 30, 1986, A--- transferred substantially all of its assets to R---, Inc., in exchange for first issue stocks, an assumption of liability, and a note. A--- had incurred a large tax liability arising primarily from ex-tax out-of-state truck purchases. The trucks purchased were used in the nontaxable trucking business.

A--- also had a truck selling business. A--- had a seller's permit issued by us and a DMV license to sell vehicles. Some truck leasing transactions were taxes as sales at their inception. A--- also disposed of used vehicles from its trucking business fleet.

A notice of successor liability was issued to R---, based upon the purchase price for the entire enterprise.

It has been apparent to us since at least April 1988 that there is something wrong with our assessment. What is wrong is this: Revenue and Taxation Code sections 6811 and 6812 have not historically been applied by the Board in circumstances where someone purchased the assets of a service business. Here A---' business was primarily a trucking business and only incidentally and secondarily a truck selling business. R---, Inc., purchased the trucks and tractors used in the trucking business, but this property cannot be characterized as assets of the truck selling business. If these were assets of the truck selling business, they would be inventory. They were not inventory; they were the capital assets of the trucking business. At best, here

R---, Inc., purchased a truck selling business and a trucking business. Its liability under Revenue and Taxation Code sections 6811 and 6812 would be limited to the purchase price paid for the truck selling business assets.

The original contract price was \$6,323,800. As a result of adjustments for a discount and for two individual tractors, the price was reduced to \$6,032,249. Of this purchase price, the price for the revenue equipment was \$5,922,249. R---, Inc., paid \$10,000 to acquire the operating authority and \$50,000 to purchase materials and supplies used in the trucking business. Thus the purchase price for the truck selling business was as follows:

\$	24,000.	Leasehold improvements
\$	7,500.	Furniture/office equipment
\$	10,000.	Shop/garage equipment
\$	<u>8,500.</u>	Furniture/office equipment
\$	50,000.	Total

Thus, R---'s maximum liability under sections 6811 and 6812 is \$50,000.

The tax liability generated by the truck selling business (as opposed to the trucking business) was \$250,755.74. R--- is the successor with respect to this liability, but the purchase price paid with respect to the business which generated this liability was \$50,000. Accordingly, it is our recommendation that the successor billing should be reduced to \$50,000.

This matter should be taken off the hearing agenda. We understand that taxpayer concurs in our recommendation. This matter can be disposed of on the nonappearance calendar. We recommend that the Petition Unit write to the taxpayer and to the Appeals Unit, advising each that the Business Taxes Department has changed its position. We have discussed this matter with Mr. Charles Cordell, and he is in agreement with our analysis.

GJJ:ar

cc: Mr. Charles Cordell  
Mr. Lawrence A. Augusta  
Ms. Janice Masterton