State of California

Board of Equalization
Legal Division

M e m o r a n d u m

545.0048

To : Audit Review and Refunds (JWC)

Date : October 20, 1983

From : Legal (DJH)

Subject :

This is in reply to your memorandum of September 13, 1983 asking our opinion on the application of sales and use tax to a _____ claim for refund (claim No. _____). The claim is based on Regulation 1701(b)(1) which states that a deduction for tax paid purchases resold should be taken if "The retailer when making the purchase intends to use the property rather than resell it, but later resells it before making any use thereof."

On selling various assets from its _____ and on shutting down its _____, _____ had no further use for the associated repair or replacement parts which had been purchased tax paid or on which use tax had been paid. Such parts were resold from _____ stores inventory and now _____ claim No. _____ requests a refund. Oakland Auditing asks whether the tax paid purchases resold deduction is available given such facts.

Implicit in Oakland's inquiry is the question of whether such repair or replacement parts should be considered as in "standby service" [Regulation 1701(c)] while in the stores inventory, thereby precluding a tax paid purchases resold deduction. Oakland Auditing attached a copy of my December 11, 1973 memo to Mr. Robert Nunes, presently Chief of Field Operations, which recommended allowing a _____ claim for refund under very similar, if not identical, facts.

In our opinion, _____ claim No. _____ should be granted as to the repair or replacement parts resold after only storage. In effect, nothing has changed since my 1973 memo to Mr. Nunes. There is still something of an ambiguity (some would say a contradiction) between Regulation 1701(b) (1) and Regulation 1701(c). While it is easy to say that a fire extinguisher which is hung on a wall in case of fire but is never actually used to extinguish a fire, the classic example, is sufficiently used in standby service to preclude a tax paid purchases resold deduction, we have never been heroic enough to apply the same standby theory to all repair or replacement parts, and I think with good reason. While the distinction between such a fire extinguisher and spare parts is hard to verbalize as it relates to "use", such distinction is there and we all recognize it.

Since my memo of December 11, 1973 to Mr. Nunes, the application of the standby rule to spare parts has been studied, at least as to the airline industry. I have been unable to locate a copy of the study itself, but I am attaching a copy of then Principal Auditor Don Brady's April 25, 1978 memo to then Assistant Chief Counsel Tom Putnam which summarizes the report and Mr. Putnam's

memo of May 2, 1978 to the Honorable Richard Nevins which concludes that "it does not seem necessary or advisable to amend a regulation to broaden the application of the standby theory with respect to parts inventories of airlines."

Of course, the question is an easier one as to those airlines that do repair work for other airlines. Arguably the conclusion could be different as to taxpayers who do not resell parts in the regular course of business. Nevertheless, I believe our position is the same whether or not parts are resold in the regular course of business, i.e., we do not apply the standby theory to spare parts inventories. To do so would probably require an amendment to Regulation 1701 as mentioned in Mr. Putnam's memo. I detect no support for such an amendment at this time.

DJH:rar

Attachments

cc: Mr. Robert Nunes