

M e m o r a n d u m**550.0076**

To: --- -- Auditing (CO)

Date: October 29, 1985

From: Headquarters -- Legal (JEM)

Subject: [Name]
SR -- XX XXXXXX

This is in reply to your September 23, 1985 memo to Mr. Hennessy regarding Regulation 1620.2.

We understand that this taxpayer operates a cruise ship on Lake Tahoe. All cruises begin and end at [name], Nevada, approximately --- miles from the California border. Many of the cruise routes extend through California waters, and in fact are primarily inside this state, but the ship never lands or docks at a California location. Customers pay a lump sum amount for each cruise.

The ship's bar serves beverages on all cruises. Some cruises include meals as well. The lump sum charge for the cruise usually entitles the customer to one or two drinks, plus the meal if one is offered. Additional drinks can be purchased at any time for a separate charge. In a recent audit, you found that \$361,900 in beverage sales (approximately 70 percent of total beverage sales) occurred while the ship was in California waters. The taxpayer is licensed to sell alcoholic beverages in this state. (License #XX-XX-XXXX)

1. Is the taxpayer a "carrier" under Regulation 1620.2?

Yes. Subdivision (b)(1) of the regulation defines "carrier" as "any person or firm who engages in the business of transporting by vehicle, train, vessel, or aircraft persons or property for hire or compensation." While the purpose of these cruises may be entertainment rather than transportation, the taxpayer does transport people by vessel for compensation, and therefore comes within the definition. (See Barr v. Venice Giant Dipper Co. Ltd., 138 Cal.App. 563, where the operator of a "miniature scenic railway" or roller coaster was held to be a carrier.)

2. Are beverages sold at the ship's bar and during meals exempt from tax?

Yes. Subdivision (b) of the regulation provides that tax applies to sales of taxable beverages in this state by carriers "except when the sale...occurs during a trans-state trip." Subdivision (a)(2) defines "trans-state trip" as "the act of crossing California territory or airspace during a continuous journey between points outside this state without stopping or landing in this state."

The statutory basis for exemption is Revenue and Taxation Code Section 6352, which exempts all transactions that California cannot constitutionally tax. The reasoning is that "trans-state trips" do not provide sufficient "nexus" to permit taxation. While these cruises all begin and end at one point, this does not increase the taxpayer's California connections. Accordingly, the cruises are "trans-state trips" and the sales of beverages are therefore exempt.

3. Is the exemption retroactive?

Yes. Revenue and Taxation Code section 7051 authorizes the Board to prescribe when regulations are to be applied without retroactive effect. Since the Board did not do so in adopting Regulation 1620.2, the regulation applies retroactively. We also note that, according to staff comment presented to the Board at the adoption hearing, the regulation was intended to clarify and not to change existing law.

4. Are the meals also exempt?

Yes. While the regulation does not mention meals, for "nexus purposes we see no reasonable distinction between sales of beverages and sales of meals.

JEM:ba