

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

570.1115

APPEALS DIVISION

In the Matter of the Petition)	HEARING
for Redetermination Under the)	DECISION AND RECOMMENDATION
Sales and Use Tax Law of:)	
)	
C--- AIRLINES, LTD. -)	No. SY -- XX-XXXXXX-010
THE A---)	
)	
<u>Petitioner</u>)	

The above-referenced matter came on regularly for hearing before Hearing Officer Susan M. Wengel on March 7, 1991 in Culver City, California.

Appearing for Petitioner:	J--- S. B---
	Certified Public Accountant
	L. P. L---
	Certified Public Accountant
	J--- Y---
	Auditor for C--- Airlines

Appearing for the Sales and Use Tax Department:	Sally A. Phetteplace Supervising Tax Auditor
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Protested Item

The protested tax liability for the period July 1, 1985, through September 30, 1988 is measured by:

<u>Item</u>	<u>State, Local and County</u>
A. Ex-tax consumable supplies transferred to company headquarters in Taiwan to California locations.	\$357,604

Contentions of Petitioner

1. Disposable food supplies such as paper plates, plastic bowls, cups, flatware and napkins should not be subject to use tax because they are not utilized by the passengers until the meals are served during flight outside of California.
2. Passenger comfort supplies given to first class and business flight passengers are not used until the airplane is in international airspace

Summary of Petition

Petitioner is a corporation which is engaged in business as a foreign air carrier operating out of San Francisco and Los Angeles. During an audit by the Sales and Use Tax Department (Department), the auditor ascertained that certain disposable trays, bowls, flatware and the like had been shipped into California from Taiwan and stored in duty free warehouses. Petitioner contracts with A--- International B--- to cater its in-flight meals. AIB prepares the food, places it on petitioner's trays with petitioner's cups, bowls, flatware and napkins, and delivers the meal trays to the airplane. When AIB needs supplies from petitioner's warehouses, petitioner's personnel arrange for a bill to be drawn which authorizes the release of the goods without tax being paid. The Department takes the position that once petitioner authorizes the caterer to unpack the food supplies and use the products to prepare a meal tray, that a taxable use takes place in California.

Petitioner contends that the disposable food supplies are used by the passengers outside of California and that Revenue and Taxation Code Section 6009.1 exempts the storage of these products.

The Department further asserts that the passenger comfort items such as razor blades, eye shades and slippers are taxable because these items were also first stored in the duty free warehouse and then delivered to the flight crew for disposal at their discretion. The Department's position is that a taxable use takes place in this state as the flight crew has control over the items.

Petitioner again contends that Section 6009.1 applies and that no use is made of the comfort items until the aircraft is in flight. AIB testified at the Appeals hearing that the flight crew is instructed not to give out the travel kits until after take-off.

The Department computed the protested measure by conducting a test of 1987 non-revenue way bills which were projected on a quarterly basis throughout the audit period. These projections were then adjusted for consumable supplies reported by petitioner on an estimated basis. Petitioner is not protesting the tax due on printed matter, timetables, luggage

tags and the like which are examples of office supplies consumed by petitioner in the daily operations of its business here in California

Analysis and Conclusions

The first issue is whether petitioner made a taxable use of the trays, flatware, plates, bowls and the like when it allowed these items to be released to a caterer for preparation of its meal trays. Revenue and Taxation Code Section 6201 imposes a use tax on the storage, use or other consumption in this state of tangible personal property purchased from any retailer for storage or use in California. What is a “use” is also defined in California law. Revenue and Taxation Code Section 6009 provides:

“‘Use’ includes the exercise of any right or power over tangible personal property incident to the ownership of that property, and includes the possession of, or the exercise of any right or power over, tangible personal property by a lessee under a lease, except that it does not include the sale of that property in the regular course of business.”

The Department appears to rely on the case of Parfums-Corday, Inc. v. State Board of Equalization (1986) 187 Cal.App3d 630 in imposing a use tax on petitioner’s assemblage of the meal trays in California. In this case, the court held that Max Factor was the consumer of promotional displays it purchased from manufacturers under resale certificates. They stored the items in their Los Angeles warehouse, assembled them into prepacks, and shipped them to their customers without making a separate charge or increasing the cost of the merchandise placed in the prepacks. The court concluded that Max Factor made a gift of the displays to its customers and that this was a taxable use in California when delivery was made to the common carrier. In other words, the property had some functional purpose in California other than to serve as a mere object in transit.

In the present case, petitioner through its agent retained possession of the items while they were in California. The only use made was to take the individual items and assemble them with food products to form a meal tray. Revenue and Taxation Code Section 6009.1 provides that:

“‘Storage’ and ‘use’ do not include the keeping, retaining or exercising any right or power over tangible personal property for the purpose of subsequently transporting it outside the state for use thereafter solely outside the state, or for the purpose of being processed, fabricated, or manufactured into, attached to or incorporated into, other tangible personal property to be transported outside the state and thereafter used solely outside the state.”

As the only use petitioner made of the items was to assemble the items on meal trays, we must conclude that Section 6009.1 applies and that no use tax is applicable. As the Parfums court stated, there is not taxable use if the property has no function in California other than to move through the state for consumption elsewhere. (Parfums-Corday, Inc. v. State Board of Equalization, supra 187 Cal.App3d at p. 638.)

It is well to note that if any of the items used to prepare meal trays are items which can be reused in California such as stainless silverware, cloth table napkins, glasses or the like, the use by petitioner to assemble the trays will be subject to tax. Section 6009.1 requires that the property thereafter be used solely outside of California.

Petitioner further indicated that because it sold the meals to its passengers, the supplies should be exempt just like the meals. This position is incorrect. While meals sold to airlines are exempt from sales tax pursuant to Revenue and Taxation Code Section 6359.1 as food for human consumption, the airlines are considered to be the consumers of all other items furnished to their passengers where no separate charge is stated. (Sales and Use Tax Annotation 550.0040 dated October 22, 1964.)

The final issue involves the taxability of convenience items given to first class or business class passengers. Petitioner's personnel have testified that usually these items are on the airplane before the airplane even arrives in California. On occasion, however, the flight crew will need more of these travel kits and will request that the items be released from the bonded warehouse. The release will be authorized by petitioner and the kits are delivered to the flight crew on the airplane. At this time, a crew member has been directed to store the kits until after the in-flight meal service. The crew members, however, do have control over the kits and could give them out early to a first class passenger if the passenger was adamant in making his request. There is no evidence, however, that any of these disposable convenience items are given to the passengers in California. Quite clearly, if they were, a gift would have taken place in California and petitioner would be responsible for the use tax.

For the reasons discussed above, it is concluded that Section 6009.1 excludes petitioner's use from the definition of a taxable use.

Petitioner has noted the Uniform Local Sales and Use Tax Annotation 715.0230 excludes from local tax all food service and commissary supplies reasonably necessary for the sustenance of passengers in flight. Petitioner asserts that this local tax exclusion should be expanded. There is not, however, a similar exclusion in the Sales and use Tax Law and without specific statutory authority no relief can be recommended. It should be pointed out that the above-referenced local tax annotation does not affect the taxability of travel kits as these items are not considered to be "directly used."

Recommendation

It is recommended that the audit staff ascertain if any of the meal service items were nondisposable items and if any of the convenience items were given to the passengers prior to take off. If neither of these factual situations are present, then the petition should be granted.

Susan M. Wengel, Hearing Officer

April 29, 1991

Date