

STATE OF CALIFORNIA

395.0009

BOARD OF EQUALIZATION

BUSINESS TAXES APPEAL REVIEW SECTION

In the Matter of the Petition)	
for Redetermination and the)	DECISION AND RECOMMENDATION
Claims for Refund Under the)	
Sales and Use Tax Law of:)	
)	
)	
THE D--- M--- G---, INC.)	No. SR --- XX-XXXXXXX-010
)	
)	
<u>Petitioner</u>)	

The Appeals conference in the above-referenced matter was held by Senior Staff Counsel H. L. Cohen on April 15, 1992, in San Diego, California.

Appearing for Petitioners:

Mr. J. T---
Controller

Mr. R. C---
Attorney at Law

Appearing for the Sales and
Use Tax Department:

Ms. M. Reilly
Tax Auditor
San Diego District

Protested Item

The protested tax liability for the period January 1, 1987 through March 12, 1990 is measured by:

<u>Item</u>	<u>State, Local and County</u>
A. Unreported sale of computer programs	\$700,000

Contention

Petitioner contends that the sale in question was an exempt occasional sale.

Summary

Petitioner is a corporation which was engaged in providing computer consulting services with sales of computer hardware and software. It began in business in July 1985. There has been no prior audit. This audit was a close-out audit occasioned by the sale of the business assets.

On March 12, 1990, petitioner sold all of its assets to B--- S---, Inc. Included in the sale were 13 computer programs used by petitioner in the conduct of its business. Three of these programs were pre-written and 10 were programs which had been specifically designed for petitioner's use. The lump-sum sales price for the 13 programs was \$700,000. The auditor, relying on Touche Ross & Company v. State Board of Equalization, 103 Cal.App.3d 1057, concluded that these computer programs were not custom computer programs when sold by petitioner. The sale of the programs was therefore regarded as subject to tax.

Petitioner points out that in the Touche Ross case, the court stated that "most secondary sales of custom computer programs designed to the special order of the selling party come within the occasional sale exemption created by Sections 6367 and 6006.5(a)". Petitioner contends that the sale of the programs constituted an occasional sale because petitioner's principal business operation for the 12 months preceding the sale of assets consisted of custom programming and consulting which do not require the holding of a seller's permit.

Petitioner had made no sales of tangible personal property during the first two calendar quarters of 1989. In December 1989, petitioner made 14 individual sales of used computers and related hardware. The total amount of these sales was \$14,520. The equipment sold in these 14 sales had previously been sold in a single sale of a system to I--- V---, but had been repossessed. After the repossession, the individual components were separately sold. In August 1989, petitioner sold two complete systems to B--- & T--- for \$5,000.

Petitioner contends that it had no choice as to the repossessed equipment and that the disposal of this equipment should be viewed as a single liquidation sale. Petitioner contends that the sale to B--- & T--- should be regarded as insubstantial. If the sale of the repossessed equipment is regarded as a single sale and the B--- & T--- sale is disregarded, then the final sale of assets would be regarded as an occasional sale because petitioner would not be a retailer under the "three sale" rule of Section 6019 of the Revenue and Taxation Code. Petitioner also contends that it is unfair that a relatively small amount of earlier sales should trigger a large tax liability at a later time.

Analysis and Conclusions

Section 6367 of the Revenue and Taxation Code exempts occasional sales from tax. Section 6006.5 defines "occasional sale" to include the sale of property not held in the course of activities which require the holding of a seller's permit. Sales and Use Tax Regulation 1595 provides in pertinent part of subdivision (a)(1):

"Generally, a person who makes three or more sales for substantial amounts in a period of 12 months is required to hold a seller's permit. A person who makes a substantial number of sales for relatively small amounts is also required to hold a seller's permit.

"Tax does not apply to a sale of property held or used in the course of an activity not requiring the holding of a seller's permit unless the sale is one of a series of sales sufficient in number, scope and character to constitute an activity for which the seller is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state."

The portion of the decision in Touche Ross cited by petitioner deals with businesses which do not sell tangible personal property. For example, an accounting firm which sells all of its assets in a single sale would not be taxable on the secondary sale of its custom computer programs. The question to be decided here is whether petitioner should be regarded as a seller of tangible personal property. If petitioner is regarded as a seller of tangible personal property, then the tax is properly applied to the sale of the programs in question.

Subdivision (a)(5)(B)2 of the regulation provides that where a service enterprise and a sales business are operated together so as to constitute one business, tax will apply to the sale of the assets of the business. Petitioner's consulting activities and its sales activities unquestionably constitute a single business. Although petitioner made few sales of tangible personal property during the 12-month period immediately preceding its asset sale, it was not because petitioner was not in the business of selling tangible personal property. It was because none of petitioner's customers during that period wished to buy hardware from petitioner.

Looking to the "three sale" rule, there is no basis to regard the 14 sales of repossessed equipment as a single sale. There were 14 individual customers. I regard 14 sales of hardware in one month to be a substantial number of sales. I do not regard the \$5,000 sale to B--- & T--- as being for an insubstantial amount.

I conclude that petitioner was a seller of tangible personal property, both from the fact that it was in the business of selling hardware and from the fact that it made substantial sales of hardware both in quantity of sales and the dollar value of sales.

While it is unfortunate that the sales in question triggered a tax liability in excess of the amount of the sales, that is no basis under the law for granting relief.

Recommendation

Deny the petition. Deny the related protective claims for refund dated July 27, 1990 and July 17, 1990.

H. L. Cohen, Senior Staff Counsel

5-22-92
Date