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June 15, 1994

BURTON W. OLIVER
Executive Director

X-----

Gentlemen:

This is in reply to your January 17, 1994 letter regarding the application of sales tax to the transfer of a software product known as X----- from X-----, a California corporation, X----- to X----- a Texas Corporation, X----- pursuant to Assets Purchase Agreement, dated October 11, 1993. You provided the following facts:

"The X----- assets (Software, Technology, Marks, Contracts, Sales and Marketing Materials, customer information, including the Customer List, Equipment, Inventory and chooses in action related to occurrences before the Closing) are specified in Section 1.1 of the Agreement and on Schedules 1.1(a), 1.1(b), 1.1(c), 1.1(d), 1.1(e), 1.1(f), 1.1(g) and 1.1(h) attached to the Agreement. The Excluded Assets, which are specified in Section 1.4 of the Agreement and on Schedule 1.4, were not conveyed to Purchaser. The principal asset that was acquired by Purchaser is the Software and Technology, including, most importantly, the source code versions of the Software necessary to compile the object code versions of the Software. Accordingly, the parties allocated most of the Purchase Price to the Software and Technology, as shown on Schedule 7.5 under the description X----- Asset Intangibles."

Ms. X----- sent us a copy of the Agreements. We did not receive a copy of the schedule.

Pursuant to Section 7.4 of the Agreement, X----- transferred to X----- the software by electronic means as described in an affidavit of Mr. X----- which describes the procedure as follows:

"On behalf of X----- I participated in the transmittal of all of the Software and Technology which was embodied in computer programs, including the source code versions of the Software, and the manuals, disks and other "softcopy" items which were included in the Software, Technology and Sales and Marketing Materials (collectively, the "Code") by electronic means as described in Paragraph 5 of this affidavit. X----- --, on behalf of Seller, also participated in the transmittal procedures.

“5. The transmittal took place on October X----- at Seller’s business premises in X-----, California. The following procedures were followed in connection with the transmittal of the Code stored on the hard disk media of Seller’s X----- computer (“Seller’s X-----”) to the hard disk media of Purchaser’s X----- (“Purchaser’s X-----”) and the transmittal of the Code stored on the hard disk media of Seller’s Macintosh IIFX Server (“Seller’s Macintosh”) to the hard disk media of Purchaser’s Macintosh computer (“Purchaser’s Macintosh”):

- (i) The files on Seller’s X----- and Seller’s Macintosh were readied for transmittal by myself and Seller’s employees.
- (ii) A standard computer cable was used to connect Seller’s X----- with Purchaser’s X-----.
- (iii) A standard computer cables was used to connect Seller’s Macintosh with Purchaser’s Macintosh.
- (iv) The Code stored on the hard disk media of Seller’s X----- was transmitted over the computer cable from Seller’s X----- to Purchaser’s X----- for storage on the hard disk media of Purchaser’s X-----.
- (v) The Code stored on the hard disk media of Seller's Macintosh was transmitted over the computer cable from Seller's Macintosh to Purchaser's Macintosh.
- (vi) Together with Seller's employees, I verified that the Code that had been transmitted to Purchaser's X----- and Purchaser's Macintosh, respectively, had, in fact been successfully transmitted. In order to verify the transmission, we compared the version contained on Seller's X----- and Seller's Macintosh, respectively, with tapes and floppy disks of known quality to determine equivalence and we successfully compiled object code versions of the Software from the source code versions of the Software.
- (vii) Upon completion of the transmission and prior to the closing of the sale to Purchaser, Seller's employees deleted all Code that was purchased from Seller pursuant to the Agreement from Seller's X----- and Seller's Macintosh.
- (viii) At erasing, Purchaser purchased leased Seller's Macintosh from X-----.
- (ix) After closing, purchaser leased seller's Macintosh from X-----.
- (x) This completes the transfer operation."

Your letter notes that the method of electronic transfer used by X----- in the present transaction was in aspects identical to the procedure described X----- by Assistant Chief Counsel Gary J. Jugum X-----. The conclusion Mr. Jugum reached in his letter was based on facts showing the seller retained control over the seller's computer, and the purchaser retained control of its computer. In that case, if the seller transmitted the data to the volatile memory of the purchaser's computer, the seller did not transfer tangible personal property to, nor

fabricate tangible personal property for, the buyer under Revenue and Taxation Code section 6006. Therefore, the transaction would not be a "sale" for purposes of the Sales and Use Tax Law.

Assuming that such is the case under the facts of the transfer by X-----, the transfer is not subject to sales tax.

You note that, since the purchaser has certified to the seller that it has acquired the inventory items for resale in the regular course of business, the transfer of inventory should be a nontaxable transaction. We agree, provided the purchaser's certification meets the requirements to qualify as a resale certificate under Sales and Use Tax Regulation 1668, Resale Certificates.

The sale of tangible personal property sold to the purchaser was exempt when the seller shipped the property by common carrier to X----- Texas pursuant to the contract.

The charge for contracts and choses in action is nontaxable. Assuming the transfer of the rights to trademarks and servicemarks does not involve the sale of artwork, the charge is nontaxable.

We hope this answers your questions; however, if you need further information, feel free to write again.

Very truly yours,

Ronald L. Dick
Senior Tax Counsel

RLD:plh