CALIFORNIA STATE BOARD OF EQUALIZATION

APPEALS DIVISION SUMMARY FOR BOARD HEARING

In the Matter of the Petitions for Reallocation of Local Tax Under the Uniform Local Sales and Use Tax Law of:	)	
CITIES OF ONTARIO, PALM SPRINGS, SAN DIEGO, SANTA BARBARA, and COUNTIES OF SACRAMENTO, SAN MATEO	)	Case ID's 525325, 525326
Petitioners	)	

Taxpayer:	Seller of jet fuel
Dates of Knowledge:	08.02.04, 12.21.04
Allocation period:	03.01.04 – 12.31.07
Amount in Dispute:	$12,276,670
Notified jurisdiction:	Oakland

This appeal was scheduled for Board hearing on November 19, 2013, but was postponed at Oakland's request because its representative was not available that day. The hearing was then rescheduled for December 18, 2013, but was deferred at the request of the Appeals Division in order to issue a Supplemental Decision and Recommendation (SD&R) to address Oakland's Request for Reconsideration. This appeal involves an amount in controversy that is $500,000 or more and thus is covered by Revenue and Taxation Code section 40, as explained below.

BACKGROUND

Taxpayer sells jet fuel primarily to its parent. These sales were delivered to parent's aircraft at California airports from storage tanks located within the same local taxing jurisdiction except that fuel delivered to aircraft at San Francisco International Airport (SFO), which is located in the unincorporated area of San Mateo County, was delivered from storage tanks located in South San Francisco. Taxpayer reported the tax on the sales in dispute as sales tax and directly allocated the local tax to Oakland based on the view that its Oakland office was the place of sale.[1] If the allocation is

[1] This office was opened after parent entered into a 10-year Economic Development Agreement with Oakland under which parent received 65 percent of the local sales tax taxpayer reported to Oakland. This office was closed midway through 2008.

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upheld, parent would keep the payment it received from Oakland of 65 percent of the tax Oakland received from sales made by taxpayer.[2]

The Cities of Ontario, Palm Springs, San Diego, and Santa Barbara, and the County of Sacramento (petitioners) filed petitions received on August 2, 2004, seeking direct reallocation to the respective petitioners of local tax derived from taxpayer's jet fuel sales at Ontario International Airport, Palm Springs International Airport, Sacramento International Airport, San Diego International Airport, and Santa Barbara Municipal Airport. If these petitions were granted, local tax of $2,081,494 would be reallocated: $181,355 to Ontario; $20,474 to Palm Spring; $1,194,331 to San Diego; $414 to Santa Barbara; and $684,920 to Sacramento County. The County of San Mateo (San Mateo[3]) filed a petition received on December 21, 2004, seeking direct reallocation of local tax derived from taxpayer's jet fuel sales at SFO. If this petition were granted, local tax of $10,195,176 would be reallocated to San Mateo.

The Sales and Use Tax Department (Department) denied the petitions based on its determination that taxpayer had an office in Oakland that participated in the sales of jet fuel to parent and that such office was required to hold a seller's permit. Petitioners and San Mateo timely appealed.

An appeals conference was held on August 10, 2010,[4] and we found in our September 12, 2012 Decision and Recommendation (D&R) that use tax applied to the subject sales, and not sales tax, because taxpayer's office in Oakland did not participate in the sales. The D&R recommended that the disputed local tax taxpayer had allocated to Oakland be reallocated directly to San Diego and San Mateo (granting their petitions in full) and be reallocated indirectly to Ontario, Palm Springs, Santa Barbara, and Sacramento County through their respective countywide pools (granting their petitions in

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[2] We have therefore taken this direct financial interest into account when examining the credibility of any statements made by or on behalf of parent or taxpayer.

[3] Even though San Mateo County is a petitioner and the primary contentions of all petitioners are essentially the same, because San Mateo County and the other petitioners have some alternate contentions different from each other, to avoid confusion, when we use the term "petitioners" below, we refer to all petitioners except San Mateo County, whom we refer to as San Mateo.

[4] Under the provisions of California Code of Regulations, title 18, section 1807 in effect at the time, Oakland did not receive notice of the appeals conference because it was not "substantially affected" by the Department's decision to deny the petitions. (Former Cal. Code Regs., tit. 18, § 1807, subd. (c)(2).) The regulation has since been amended to provide that a jurisdiction that *would be* substantially affected if any petition were granted receives notice of the appeals conference. (Cal. Code Regs., tit. 18, § 1807, subd. (c)(2).)

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part[5]). A hearing was timely requested by Oakland, contending that the local tax was properly allocated to Oakland.[6] A hearing was also timely requested by the petitioners for whom we recommended indirect reallocation. Thereafter, Oakland requested that we reconsider the D&R after holding another appeals conference at which Oakland could participate. We agreed to do so.

The second appeals conference was held on July 28, 2014. In our September 25, 2015 SD&R, we reversed our prior finding based on additional evidence, and we found instead that receipt of purchase orders by the Oakland office constituted participation by that office for purposes of California Code of Regulations, title 18, section (Regulation) 1620, subdivision (a)(2)(A). Accordingly, since the sales occurred in California, we concluded that the applicable tax was sales tax. Since we also found that taxpayer's Oakland office was its only business location in California and was required to hold a seller's permit under Regulation 1699, we concluded that the local sales tax was correctly allocated directly to Oakland. The SD&R therefore recommends that the petitions be denied. A hearing was timely requested by petitioners and San Mateo, disputing our conclusion that the local tax was properly allocated to Oakland.

UNRESOLVED ISSUE

Whether taxpayer correctly allocated the local tax as sales tax to the office located in Oakland. We conclude that the local tax was correctly allocated to Oakland.

The Department determined that the disputed local tax was sales tax because the sales occurred inside California with participation by taxpayer's Oakland office and the local sales tax was correctly allocated directly to Oakland because taxpayer's Oakland office was required to hold a seller's permit. In support of this determination, the Department relies on emails received from taxpayer that, in general, establish that taxpayer's employee who was located at the Oakland office (Ms. M) performed various activities, including the receiving of purchase orders, which taxpayer and its parent called

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[5] The D&R found that the general rule that use tax is indirectly allocated through the applicable countywide pools applied, rather than direct allocation under California Code of Regulations, title 18, section 1802, subdivision (d)(1), because the subject transactions were not $500,000 or more (i.e., local use tax of $5,000 or more).

[6] Since Oakland became substantially affected by the issuance of the D&R (Cal. Code Regs., tit. 18, § 1807, subd. (a)(6)) and became a notified jurisdiction (Cal. Code Regs., tit. 18, § 1807, subds. (a)(7), (c)(4)) when we mailed it a copy of the D&R, Oakland gained appeal rights in this dispute.

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"nominations," for sales made under master contracts.[7] Oakland argues that whether or not the nominations were estimates should not make a difference since they were the mechanism by which the customer notified taxpayer of the amount of fuel it wanted delivered to a specific location for transfer to its aircraft and thus Ms. M's receipt of the nominations from taxpayer's customers was participation in the sales.

Petitioners and San Mateo primarily contend that taxpayer's Oakland office did not participate in the sales and thus the use tax applies.[8] They assert Ms. M's actual role was to purchase sufficient inventory of fuel to meet projected demand, an activity that had no meaningful effect on the sales transaction itself (i.e., a precursor to delivery to taxpayer and not part of the sale from taxpayer to parent) and which thus did not constitute participation in the sales. Petitioners and San Mateo argue that the nominations were not purchase orders and did not obligate parent to purchase any particular quantity of fuel; instead, they argue that the estimates provided Ms. M the information she needed to arrange for sufficient fuel to be available at each location in a given month to satisfy parent's requirements.[9] Petitioners further argue that the actual purchase orders were the delivery tickets issued

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[7] Each master contract required parent to submit by facsimile to taxpayer's Oakland office what the contract characterizes as a purchase order. However, since taxpayer and its parent refer to such documents as "nominations," for consistency with statements from taxpayer and parent we generally use the same term below.

[8] Alternate contentions were propounded by petitioners and San Mateo.

Petitioners' alternate contention is that the locations of the storage tanks were business locations of taxpayer that participated in the sales. They assert that, even if taxpayer's Oakland office had negotiated the contracts, the local tax should be allocated to the wing tip locations under Regulation 1802,subdivision (b)(6)(A) (where the retailer has more than one place of business in this state and the principal negotiations are conducted at the retailer's place of business in this state). Otherwise, petitioners argue that, if taxpayer's Oakland office had participated in the sales but not negotiated the contracts, the local tax should be allocated under Regulation 1802, subdivision (a)(2)(B) to the storage locations if delivery of fuel at the storage tanks were the more significant participation.

San Mateo's alternate contentions are that: (1) tax on sales of jet fuel for delivery to aircraft at SFO should be allocated to San Mateo under the Anti-Head Tax Act (49 U.S.C. S 40116); (2) the Legislature intended all local sales tax on sales of jet fuel to be allocated under former Revenue and Taxation Code sections 7204.03 and 7205 (wing tip rule); (3) An unrelated supplier sold the jet fuel directly to parent since taxpayer never took title to the jet fuel delivered to parent's aircraft, meaning that the sales should be allocated under the wing tip rule; and (4) transactions between taxpayer and parent should not be recognized as valid sales because taxpayer lacks a separate identity from parent, meaning that the sales should be regarded as having been made by the unrelated supplier directly to parent and allocated under the wing tip rule.

As explained in the D&R, we found all these alternate contentions to be without merit. We fully addressed and rejected each of these contentions in the D&R. Although petitioners and San Mateo preserved these arguments "for the record," they have neither provided anything further in support nor specifically addressed any perceived errors in our analysis.

[9] San Mateo contends that even if it is determined that the Oakland office did participate in the sales, this could not have occurred prior to February 1, 2005, the date of the contract signed by Ms. M. San Mateo contends that Ms. M could not have negotiated the prior contract, dated March 1, 2004, because she was not hired until March 8, 2004.

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by a third-party operator located on-site at the airport (these delivery tickets were issued *after* the fuel was delivered into the aircraft).

A sale is subject to sales tax only if that sale occurs in California and there is some participation in the sale by a California location of the retailer. (Cal. Code Regs., tit. 18, § 1620, subd. (a)(2)(A).) The use tax applies unless both answers are yes. (Rev. & Tax. Code, §§ 6051, 6201.) The same rules are applicable to determine whether the local tax is sales tax or use tax. (Rev. & Tax. Code, §§ 7202, 7203; Cal. Code Regs., tit. 18, § 1803.) Where the local tax is sales tax, that tax is allocated to the place of sale. (Rev. & Tax. Code, § 7205; Cal. Code Regs., tit. 18, § 1802, subd. (d).) Such place of sale generally receives a direct allocation if that location qualifies for issuance of a seller's permit under Regulation 1699, but otherwise, the local sales tax is indirectly allocated to the place of sale through that location's countywide pool. Where the local tax is use tax, that tax is allocated to the jurisdiction of the first functional use of the purchased property, which is usually accomplished by allocating the local use tax indirectly to such jurisdiction through its countywide pool; however, a retailer must report the local use tax directly to the jurisdiction of first functional use where the transaction totals $500,000 or more (Cal. Code Regs., tit. 18, § 1802, subd, (d)(1)). Thus, we must first determine whether the applicable local tax is sales tax or use tax.

There is no dispute here that title passed and the sales occurred in California when the jet fuel was delivered to parent, nor is there any dispute that taxpayer had a business location in Oakland. Accordingly, the applicable tax was sales tax if a California business location of taxpayer participated in the sales. Taxpayer's only business location in this state was its Oakland office.[10] Thus, if the Oakland office participated in the sales, the local tax was sales tax, and the place of sale was that office.

While Regulation 1620, subdivision (a)(2)(A) refers to specific activities that support sales tax (the taking of the order or the delivery of the purchased property), it also makes clear that the

[10] In the D&R, we rejected petitioners' alternate contention that the storage tanks were business locations of taxpayer under Regulation 1620, subdivision (a)(2)(A) because taxpayer did not own or operate the storage tanks and because taxpayer's fuel in the tanks was commingled with fuel owned by others. That is, there was no location within the tanks that held fuel solely owned by taxpayer which could be regarded as a separate and specifically identifiable location effectively controlled by taxpayer.

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necessary participation to support sales tax is not limited to those two activities, nor to the moment at which title transfers (e.g., delivery). We conclude that the participation necessary to support sales tax is an activity by a California business location of the retailer serving some real purpose in the actual sales process and involving some genuine physical interaction with the sale from that location, such as negotiating sales contracts with the customer, taking orders from the customer, approving credit, delivering goods to the customer, or billing. On the other hand, there are activities that do not constitute participation in the sale for purposes of Regulation 1620. For example, participation by a California business location of the retailer in that retailer's *purchases* of resale inventory (albeit a necessary precursor to any sales of that resale inventory) is not participation in the sale. Similarly, once the sale has occurred, activities taking place after that point in time are not participation in the sale. That is, the activity supporting imposition of sales tax on a particular sale must be tied to *that sale* (i.e., the transaction).

We found that the evidence provided, though limited,[11] established that parent did submit the nominations to the Oakland office, as required by the master contracts between parent and taxpayer. While petitioners and San Mateo contend that these nominations were estimates and not purchase orders, the master contracts required parent to submit a document explicitly defined as a purchase order that provided parent's estimated needs for the next month to the Oakland office and included a provision that stated such submission constituted parent's "unequivocal and unconditional offer to purchase" from taxpayer and bound taxpayer "to perform under the Agreement only upon physical receipt of a signed Purchase Order at the Oakland, CA location."[12] Viewing this provision in isolation, parent would have been obligated to purchase the amount specified on the nomination, and the nomination would unequivocally have been a purchase order. However, this was a provision in a requirements contract, and we agree it was intended to convey an estimate of the fuel that parent would

[11] We are disappointed that we were provided limited supporting documentary evidence and that this evidence was not provided by taxpayer or parent when their records were subpoenaed by the Department in July of 2011. Nevertheless, we do not believe taxpayer's inability to locate or its delay in the production of such evidence necessarily undermines taxpayer's credibility. Even though taxpayer has a clear financial interest that bears on its credibility and even though the submission of evidence was not as orderly, expeditious, or complete as we might like, that does not mean that the evidence that was provided is inherently untrustworthy.

[12] The actual form was incorporated by reference as an exhibit to one of the master contracts provided.

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purchase rather than specifying the *exact* amount of fuel that would be purchased. That is, although the contract itself does not explicitly state that the binding purchase order would not be exact, taking the contract as a whole, including the wording of the purchase order form actually submitted by parent to taxpayer, it is clear that the parties understood that the purchase order was not intended to bind taxpayer to sell, or to bind parent to purchase, the exact and specific amount specified on that order. Rather, the contracts required parent to submit a purchase order each month that reflected an amount of fuel that was as close to the actual amount parent would seek to purchase the next month as parent could provide, and parent was then required to purchase and taxpayer was required to sell, those actual requirements. Under these circumstances, we conclude that the nominations qualify as purchase orders for purposes of allocating local tax and, in any event, certainly constituted participation by taxpayer's Oakland office. We further reject petitioners' contention that delivery tickets issued after the purchased goods were already fully delivered to the purchaser could constitute the purchase order: receipts are not purchase orders.

Thus, we conclude that receipt of the purchase orders the parties called nominations by the Oakland office constituted participation by that office (regardless of whether they constituted purchase orders) for purposes of Regulation 1620, subdivision (a)(2)(A) and Regulation 1802, subdivision (a)(1), and that sales made pursuant to those orders were subject to state and local sales tax. We further conclude that the local sales tax was properly allocated directly to Oakland because, as a location receiving purchase orders, that office was required to hold a seller's permit. (Cal. Code Regs., tit. 18, §§ 1699, subd. (a); see Article III, paragraph B, of the Agreement for Administration of Local Sales and Use Tax.) In addition, even though Ms. M did not commence work at the Oakland office on March 1, 2004, our understanding is that another employee (Mr. H) performed the same activities from that office until he was replaced by Ms. M.[13] Accordingly, we conclude that the local tax for the entire allocation period was correctly allocated directly to Oakland and recommend that the petitions be denied.

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[13] Since we conclude that receipt of purchase orders at the Oakland office (by Mr. H and thereafter by Ms. M) constitutes participation in the sales, San Mateo's argument, that Ms. M could not have negotiated any contracts prior to signing the February 1, 2005 contract, is irrelevant.

SECTION 40 MATTER

As noted above, this matter is subject to Revenue and Taxation Code section 40. Therefore, within 120 days from the date the Board's vote to decide the appeal becomes final, a written opinion (i.e., Summary Decision or Memorandum Opinion) must be published on the Board's website. (Cal. Code Regs., tit. 18, § 5552, subds. (b), (f).) The Board's vote to decide the appeal will become final 30 days following the date on which notice of the Board's decision is mailed to the parties, except when a petition for rehearing is filed within that period.[14] (Cal. Code Regs., tit. 18, § 5561, subd. (a).)

Following the conclusion of this hearing, if the Board votes to decide the appeal, but does not specify whether a Summary Decision or a Memorandum Opinion should be prepared, staff will expeditiously prepare a nonprecedential Summary Decision and submit it to the Board for consideration at a subsequent meeting. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(2).) Unless the Board directs otherwise, the proposed Summary Decision would not be confidential pending its consideration by the Board (Cal. Code Regs., tit. 18 § 5551, subd. (b)(5)); accordingly, it would be posted on the Public Agenda Notice for the meeting at which the Board will consider and vote on the Summary Decision.

Any party may request that the Board hold in abeyance its vote to decide the appeal so the parties may review the Board's written opinion prior to the expiration of the 30-day period for the filing of a petition for rehearing. If the vote is held in abeyance, the proposed Summary Decision will be confidential until it is adopted by the Board. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(5).) Any request that the Board's vote be held in abeyance should be made in writing to the Board Proceedings Division prior to the hearing or as part of oral argument at the hearing. Any such request would then be considered by the Board during its deliberations on the appeal.

OTHER MATTERS

None.

Summary prepared by Trecia M. Nienow, Tax Counsel IV

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[14] If a petition for rehearing is filed, the Board's decision will not become final, and no written opinion under Section 40 will be considered until after the petition for rehearing is resolved.