

CALIFORNIA STATE BOARD OF EQUALIZATION
APPEALS DIVISION BOARD HEARING SUMMARY

In the Matter of the Administrative Protest)
Under the Sales and Use Tax Law of:)
STOCKTON RAILCAR REPAIR, INC.) Account Number SR KH 100-513019
Taxpayer) Case ID 493475
Stockton, San Joaquin County

Type of Business: Railcar repair

Audit period: 04/01/05 – 03/31/08

<u>Item</u>	<u>Disputed Amount</u>		
Disallowed claimed nontaxable sales	\$684,033		
Finality penalty	\$ 5,330		
		<u>Tax</u>	<u>Penalty</u>
As determined:		\$56,333.98	
Finality penalty			\$5,330.43
Less concurred		- 1,611.28	<u>00.00</u>
Balance, protested		<u>\$54,722.70</u>	<u>\$5,330.43</u>
Determined tax		\$56,333.98	
Interest through 3/31/12		23,534.43	
Finality penalty		<u>5,330.43</u>	
Total tax, interest, and penalty		\$85,198.84	
Payments		- 4,217.17	
Balance Due		<u>\$80,981.67</u>	
Monthly interest beginning 4/1/12		<u>\$ 304.01</u>	

This matter was scheduled for Board hearing in July 2011, but was deferred at the request of the Appeals Division for further review. It was rescheduled for hearing in December 2011 but was postponed at taxpayer's request to allow additional time to submit an opening brief.

UNRESOLVED ISSUES

Issue 1: Whether adjustments are warranted to the disallowed claimed nontaxable transactions. We find that no adjustments are warranted.

Taxpayer repairs railcars that are placed on the short-haul lines of Stockton Terminal and Eastern Railroad, which operate 25 miles of track within California that connect within the state to

1 tracks operated by Burlington Northern California (Burlington Northern), Central California Traction
2 Company (CCT), and Union Pacific Railroad (Union Pacific). With regard to the sales in question,
3 taxpayer made repairs and then placed the railcars on railroad lines for delivery, and it considered the
4 sales of repair parts to be nontaxable. The Sales and Use Tax Department (Department) concluded that
5 the parts in question were installed on railcars and then delivered to the customer (or customer's agent)
6 in this state, and the parts were used in this state when the railcars were placed into service on the rail
7 lines within California. Accordingly, the Department disallowed the claimed nontaxable sales of
8 repair parts at issue.

9 Taxpayer contends that all of the disallowed transactions were exempt sales in interstate
10 commerce, stating that it installed the repair parts on railcars that were empty when shipped into
11 taxpayer's facility and empty when shipped out of California. Further, taxpayer claims that the
12 railroad companies that shipped the railcars were forwarding agents pursuant to California Code of
13 Regulations, title 18, section (Regulation) 1620, subdivision (a)(3)(B). Instead of providing bills of
14 lading, taxpayer has provided a declaration signed under penalty of perjury by David Aguirre,
15 taxpayer's president, claiming that the sales of repair parts in question were exempt sales in interstate
16 commerce because the repaired railcars were delivered to a carrier or forwarding agent for shipment
17 outside this State. Alternatively, for a small percentage of the sales, taxpayer argues that the sales of
18 repair parts installed on railcars were exempt sales to common carriers for which taxpayer argues that
19 it was impossible to retain a bill of lading, as required by Regulation 1621, subdivision (c)(1), because
20 of changes in the custom of the industry.

21 Taxpayer does not dispute that the subject sales of repair parts were retail sales of tangible
22 personal property in California. As such, the subject sales were subject to sales tax absent an
23 applicable exemption or exclusion. Revenue and Taxation Code section 6396 provides an exemption
24 from sales tax for retail sales of tangible personal property which, pursuant to the contract of sale, is
25 required to be shipped and is shipped to a point outside this state by the retailer. The exemption is not
26 applicable, and sales tax applies, if the property is delivered to the purchaser in this state, whether or
27 not the purchaser's intent is to transport the property to a location in another state or foreign country
28 and whether or not the property is actually shipped to an out-of-state location. (Cal. Code Regs., tit.

1 18, § 1620, subds. (a)(3)(A) and (a)(3)(C)(1).) Bills of lading or other documentary evidence of
2 delivery of the property to a carrier, customs broker, or forwarding agent for shipment outside this state
3 must be retained by the retailer to support the claimed exemption. (Cal. Code Regs., tit. 18, § 1620,
4 subd. (a)(3)(D).)

5 With respect to the repair parts installed on railcars owned by Burlington Northern and Union
6 Pacific, the evidence shows that these parts were delivered to the carriers in California. As such, the
7 interstate commerce exemption does not apply. With respect to the repair parts installed on railcars
8 owned by out-of-state railroad companies, it is undisputed that taxpayer delivered the repaired railcars
9 to Burlington Northern, Union Pacific, or CCT, in California and that these entities meet the definition
10 of “carrier” in Regulation 1620, subdivision (a)(3)(B). However, the self-generated logs provided by
11 the taxpayer do not represent evidence sufficient to show that the repair parts sold to out-of-state
12 railroad companies were shipped outside this state prior to any use. After the D&R was issued, we
13 provided taxpayer another opportunity to provide documentation to establish that the railcars were
14 shipped out-of-state prior to any use (that is, empty). We encouraged taxpayer to submit declarations
15 by Union Pacific and Burlington Northern, including an explanation of how these companies were
16 reimbursed for their shipping services. Taxpayer provided a second declaration by Mr. Aguirre, letters
17 from Union Pacific and Stockton Terminal and Eastern Railroad, and an email from one of taxpayer’s
18 customers. The letters simply state that it is standard procedure for railcar owners to tell the railroad
19 companies where the railcars are to be shipped and that both the railcar owners and repair facilities
20 have access to a database containing information regarding the railcar’s location and destination, as
21 well as whether the railcar is to be loaded in California or out-of-state. The letters provided no specific
22 information related to the particular transactions in dispute here.

23 We find these letters give no assurance that the disputed railcars were shipped out-of-state
24 empty, nor does the customer’s email indicate whether they were. On the contrary, the email indicates
25 that Union Pacific was to ship the railcars free of charge pursuant to a lease agreement. We find this
26 actually lessens the likelihood that these railcars were shipped out-of-state empty (the free shipment
27 could have been provided in exchange for use of the railcars during that out-of-state shipment to carry
28

1 loads outside the state). Consequently, our conclusion remains that taxpayer has failed to provide
2 sufficient documentation to support its claim that the sales were exempt sales in interstate commerce.

3 The other exemption claimed by taxpayer is one for sales of tangible personal property, other
4 than fuel and petroleum products, to common carriers if the seller ships the property via the purchasing
5 carrier's facilities under a bill of lading to a point outside California. (Rev. & Tax. Code, § 6385.)
6 Any seller claiming a transaction as exempt under section 6385 must receive and retain a bill of lading
7 pursuant to which the goods are shipped by the purchasing carrier. (Rev. & Tax. Code, § 6385, subd.
8 (a); Cal. Code Regs., tit. 18, § 1621.) A bill of lading is explicitly required by section 6385. Thus, *by*
9 *statute*, the exemption is unavailable in the absence of a supporting bill of lading.¹

10 **Issue 2:** Whether relief of the finality penalty is warranted. We find relief is not warranted.

11 Taxpayer's basis for requesting relief of the finality is that it believed it did not need to file a
12 petition for redetermination because the Board would treat the audit as disputed and because its failure
13 to file a petition should be attributed to taxpayer's attorney rather than to taxpayer. We reject
14 taxpayer's assertion that it was unaware of the need to file a petition for redetermination: the Notice of
15 Determination itself informed taxpayer of its right to file a petition for determination with 30 days and
16 informed taxpayer that a finality penalty would be added unless a petition were filed or the amount of
17 tax due were paid within 30 days. We further find that, since the attorney was authorized to act for the
18 taxpayer, the attorney's failure to file a petition for redetermination should be attributed to taxpayer.
19 Thus, we find there is no basis to recommend relief of the finality penalty.

20 OTHER MATTERS

21 None.

22
23 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III
24
25

26 ¹ The exemption is based on the fiction that the common carrier purchaser will deliver the property it purchases to itself, *as*
27 *a common carrier*, and as part of that fiction, the Legislature has mandated the issuance of a bill of lading, as if the
28 purchaser were transporting a shipment from one person to another rather than taking possession of the purchased property
as the purchaser. If the common carrier industry were to conclude that the bill of lading mandate is untenable, it can of
course go back to the Legislature seeking to have the requirement replaced with a different requirement, or eliminated
altogether. In any event, the wording of the statute as applicable to the dispute here leaves no room for interpretation.