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335,0004

(916) 445-5550

March 20, 1990

Dear _____

This is in response to your letter dated February 15, 1990 regarding whether a barge you have acquired qualifies for an exemption from sales tax, which you designate as the common carrier law, section 6385.1. You state:

"The barge we are purchasing is approximately 112' by 52' in size. For at least the next 12 months it will be used as a ferry dock and a passenger loading platform. It will be tied to a pier in _____, and will be used as a platform for the ferry boat service to embark and disembark ferry boat passengers. The ferry terminal operation is under the cognizance of the City of _____ and the barge will be leased by the City for the use previously described."

In a conversation on March 6, 1990 with _____ he explained that the lease with the city is for three months with options over the next twelve months. The barge will not be used prior to its lease to the city. If the city does not terminate the lease, it will own the barge at the end of the lease term. However, the city can terminate the lease without being in default. _____ also noted that the barge will be used in the context of intrastate commerce.

Initially, I note that the proper characterization of your contract with the city is an important aspect of our analysis. If your contract is actually a sale at inception and not a true lease, sales or use tax would be applicable to your sale to the city unless that sale were specifically exempt by statute. (See Reg. 1660(a)(2)(A), a copy of which is enclosed.)

For purposes of this opinion, I assume your contract with the city is a true lease.

Revenue and Taxation Code section 6385 sets forth certain exemptions from sales tax for sales to common carriers. However, these exemptions are not applicable to the transaction about which you inquire. The only exemptions that appear relevant to this discussion are Revenue and Taxation Code sections 6368 and 6368.1, which exempt from sales or use tax the sale or lease of a watercraft which is for use in interstate or foreign commerce involving the transportation of property or persons for hire. Since the barge will not be used principally in interstate or foreign commerce, its sale to you and your lease to the city do not qualify for the exemption. (See Reg. 1594, a copy of which is enclosed.)

Since the watercraft exemption does not apply, the remaining question is whether tax is due measured by your purchase price or measured by the rentals paid by the city. The choice is yours if you make an election no later than with your timely return for the quarter in which the barge is first leased. Otherwise, the measure of tax will depend on whether the barge constitutes mobile transportation equipment (MTE) or non MTE tangible personal property. If the barge constitutes MTE (which, as discussed below, we conclude it does), tax would be measured by purchase price. That is, a lease of MTE is never a sale, and a sale of MTE which will be leased is a sale at retail. (Rev. & Tax. Code §§ 6006(g)(4), 6010(e)(4).) The lessor may, however, elect to pay tax measured by fair rental value if the lessor does so no later than with the timely return for the quarter in which the MTE is first leased. (Rev. & Tax. Code §§ 6092.1, 6094(d), 6243.1, 6244(d), Reg. 1661.)

A barge would generally be classified as MTE as defined in Regulation 1661, a copy of which is enclosed. The reason for a conclusion otherwise would be if the barge actually became part of the real estate. We would conclude that the barge became part of the real estate only if there were an intention of the owner to have the barge remain permanently attached to the pier and either the barge is attached to the pier so as to be permanent or the barge is an accessory to the pier, performing a function directly related to the pier.

Your description of the use of the barge by the city shows that it will be accessory to the pier and perform a function directly related to that pier. However, if your transaction with the city is a true lease and not a sale at inception, it seems unlikely that you, as the owner of the barge, would have an intention that the barge remain permanently

attached to the pier during the period in which you remain the true owner of the barge. Based on this, we conclude that the barge remains MTE. Based on the assumption that you have a true lease with the city and the conclusion that the barge remains MTE for the duration of that lease, if you fail to timely elect to pay your use tax liability measured by fair rental value, you will owe use tax measured by your purchase price of the barge.

We note that when you sell the barge, either to the city at the end of the lease term or pursuant to an election to purchase by the city during the lease term, or to a third party, sales or use tax will be applicable to that sale.

If you have further questions, feel free to write again.

Sincerely,



David H. Levine
Tax Counsel

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Enclosures

bc: Oakland District Administrator