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STATE BOARD OF EQUALIZATION
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Fourth District, Los Angeles

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Controller, Sacramento

CINDY RAMBO
Executive Director

July 31, 1992

[REDACTED]

Gentlemen:

Enclosed is a copy of the Decision and Recommendation pertaining to the above-referenced petition for redetermination. The Appeals Review Section recommends that the petition be granted in part and denied in part.

Please read the Decision and Recommendation carefully. If you accept the decision, no further action is necessary. If you disagree with the decision, you have the following two options.

REQUEST FOR RECONSIDERATION. If you have new evidence and/or contentions not previously considered, you should file a Request for Reconsideration. Any such request must be sent to me within 30 days from the date of this letter, at the post office box listed above, with a copy to the Principal Tax Auditor at the same box number. No special form is required, but the request must clearly set forth any new contentions, and any new evidence must be attached.

BOARD HEARING. If you have no new evidence and/or contentions, but wish to have an oral hearing before the Board, a written request must be filed within 30 days from the date of this letter with Ms. Janice Masterton, Assistant to the Executive Director, at the above post office box.

The above options are also available to the Sales and Use Tax Department. If the Department requests

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reconsideration or an oral hearing before the Board, you will be notified and given a chance to respond.

If neither a request for Board hearing nor a Request for Reconsideration is received within thirty (30) days from the date of this letter, the Decision and Recommendation will be presented to the Board for final consideration and action. Official notice of the Board's action will then be mailed to you.

Sincerely,

Stephen A. Ryan
Stephen A. Ryan
Senior Staff Counsel

SAR:ct
Enclosure

cc:

[REDACTED]
[REDACTED]
[REDACTED]
(w/enclosure)

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
(w/enclosure)

Ms. Janice Masterton
Assistant to the Executive Director (w/enclosure)

Mr. Glenn Bystrom
Principal Tax Auditor (file attached)

Out-of-State - District Administrator (w/enclosure)

STATE OF CALIFORNIA
BOARD OF EQUALIZATION
BUSINESS TAXES APPEAL REVIEW SECTION

In the Matter of the Petition)
for Redetermination Under the)
Sales and Use Tax Law of:)

DECISION AND RECOMMENDATION


Petitioner:

The Appeals conference in the above-referenced matter was held on December 19, 1991 by Senior Staff Counsel Stephen A. Ryan in Culver City, California.

Appearing for Petitioner:

Appearing for the Sales and
Use Tax Department:


Ms. Paula Gerber
Senior Tax Auditor


Mr. Gilbert Smith
Supervising Tax Auditor

Protested Item

The protested tax liability for the period October 1, 1987 through December 31, 1987 is measured by:

<u>Item</u>	<u>State, Local and County</u>
A. Unreported gross receipts from California retail sale of a 10 percent interest in the horse "Theatrical"	\$3,150,000
reaudit adj.	<u>(2,250,000)</u>
	\$ 900,000

A 10 percent penalty was added for the failure to file a tax return.

Petitioner's Contentions

1. No tax is due since no California sale occurred because the horse was sold in Kentucky on December 9, 1987 when it was located in that state at the close of the sale escrow following the occurrence of all escrow conditions.

2. An exemption pursuant to Revenue and Taxation Code 6396 applies if possession transferred in California after November 21, 1987.

3. If tax is due, relief from the penalty is appropriate.

Summary

Petitioner is and has been a partnership with [redacted] as the managing general partner.

The Board staff apparently obtained information that the thoroughbred horse [redacted] was in California in the autumn of 1987 for the Breeder's Cup race at Hollywood Park, and that petitioner, as part owner, may have then sold its ownership interests to [redacted]. An investigation was commenced. It was concluded that petitioner had made a California sale of a 35 percent ownership interest to [redacted] for \$3,150,000 on November 20, 1987 when the horse was at Hollywood Park. A Field Billing Order dated March 14, 1990 was prepared as the basis for a notice of determination which was mailed to petitioner on July 17, 1990. Following the filing of a petition for redetermination and the receipt of additional information, an Adjusted Field Billing Order dated April 12, 1991 was prepared. It reduced the tax measure by \$2,250,000 to \$900,000 on the basis that petitioner had only owned and sold only a 10 percent interest in the horse.

The Board staff found that petitioner was and had been a horse breeder and trainer located in Virginia which brought the horse into California as its expense solely for that one race. It was concluded by the Board staff that petitioner was a seller and retailer of horses at the time of the sale.

A summary of the facts supporting the Board staff's position is set forth in a memorandum dated January 2, 1990 (plus in attachments thereto) which was written by a supervising tax auditor. His memorandum reads as follows in relevant part:

"Prior to the sale, the horse was owned by the following partners:

[REDACTED]	- 50%
[REDACTED]	- 10%
[REDACTED]	- 25%
[REDACTED]	- 15%

"The horse was shipped to California (from Belmont, NY) on November 2, 1987 to compete in the Breeder's Cup race to be held on November 21, 1987 at Hollywood Park. While preparing for the race a long-running dispute between [REDACTED] and the [REDACTED] came to a head, and a compromise was reached whereby [REDACTED] would sell its interest (35%) to [REDACTED]."

"On November 20, 1987, a "Purchase and Sale Agreement" (memo A)* was drawn up and executed. It called for the sale of the interest in the horse for \$3,150,000 (the price was contingent to outcome of race). The funds were to be placed into an escrow account pending the receipt of a warranty bill of sale, the Jockey Club Registration Certificate, and confirmation that Interest was free of liens, etc. (section 4.1). Per the agreement title was to pass to the Buyer upon receipt of the two documents (section 4.2). However, the right to possession and control of the Horse passed to the Buyer upon the execution of the "Purchase and Sale Agreement" (section 7.1). Also, per the agreement the parties were to split the proceeds from the race.

"The Horse was removed from the State on November 27, 1987 (shipped by [REDACTED] to Kentucky). Escrow was closed on December 9, 1987 when the warranty bill of sale and the Jockey Club Registration certificate was [sic] delivered."

In addition to the foregoing and as further explanation, the November 20, 1987 sales agreement read as follows in relevant part:

The contracting parties were _____ as Buyer, and petitioner plus _____ as "Seller". _____ acted on behalf of petitioner and _____ . Petitioner wished to sell and _____ wished to purchase petitioner's (10 percent) interest in the horse _____ . In consideration for the agreements, promises and warranties set forth therein, they agreed to multiple terms. Petitioner agreed to sell, transfer and convey to _____ all of petitioner's right, title and interest in and to its interest in the horse. _____ agreed to purchase petitioner's interest and the 25 percent interest of _____ in the horse for a total of at least \$2,800,000, or \$3,150,000 if _____ won the Breeders' Cup Turf race to be run on November 21, 1987. _____ also agreed to pay petitioner and _____ the outstanding balance of principal and interest under a note between them dated August 20, 1985, with a \$2,000,000 payment made on November 20, 1987, and the balance within two business days of receipt of petitioner's accounting. An escrow was agreed to be opened on that day with a law firm in Louisville, Kentucky. The sale, transfer and conveyance was agreed to be made by a warranty bill of sale. Such document was to be delivered by petitioner to the escrow holder on that day. _____ was to deliver to the escrow holder a check for \$2,800,000 on November 20, 1987, plus another check for \$350,000 on November 21, 1987 if the horse won the race. Petitioner agreed to deliver to the escrow holder after the race the original Jockey Club Registration Certificate for the horse. The escrow holder was instructed by petitioner and _____ to receive from petitioner the bill of sale and the Jockey Club Registration Certificate; to receive from _____ one and possibly two bank checks covering the purchase price amount, and was also directed to conduct searches with applicable government agencies to verify the allegedly free and clear status of interests in _____, as represented therein by petitioner. Petitioner warranted not to thereafter encumber its interest in the horse. Petitioner was to be given 10 days to remove or otherwise cure any encumbrances which were discovered during the search. The escrow holder was instructed that the close of escrow was contingent upon the occurrence of those conditions. The escrow holder was instructed to deliver to petitioner the purchase price and to _____ the bill of sale and registration certificate at the close of escrow only if all the conditions had occurred. It was agreed therein that title to petitioner's interest in the horse would pass to _____ with receipt by _____ of the bill of sale and registration certificate. It was expressly written that if all the contingencies did not occur, the escrow holder was to return the funds to _____ and the documents to petitioner. They agreed that the horse would race in the colors of _____, but would remain under the training of _____.

until November 21, 1987 midnight when thereafter "shall retain his own trainer". They agreed to pay "pro-rata" the expenses previously incurred by petitioner with respect to the horse. Paragraph 7.1 read as follows:

"Any Net Earnings of the Horse from the Race will be divided pro rata based on current ownership percentages. 'Net Earnings' shall mean the gross purse earned, less jockey fee, trainer commission and stable stakes in a reasonable amount, and any entry and similar expenses relative to such race. All risk of loss, casualty and change of condition in or to the Horse shall be borne by the Buyer from the time of the execution of this Agreement forward. The right to possession and control of the Horse shall pass to the Buyer upon the execution of this Agreement."

It was agreed that any prior lease between _____ and _____ was thereby terminated. Petitioner agreed that at the time _____ paid the purchase price and when title in the horse passed to _____, a lease between _____ and _____ would automatically be assigned to _____. They also agreed that if the horse was awarded any Eclipse Award for 1987, it would be accepted jointly by petitioner, _____, and _____ with (10 percent of) the prizes, awards and trophies being the property of petitioner, and (15 percent of) the prizes, awards and trophies being the property of _____. _____ agreed to a liquidated damages clause (\$100,000 plus attorney fees and collection costs) if _____ breached the agreement. It was agreed that specific performance would be an appropriate remedy in the event of breach of the agreement since the "rights to be sold and purchased herein" were special and unique.

The check written by _____ dated November 20, 1987 to cover the \$2,800,000 purchase price was made payable to the escrow holder's trust account.

According to a Declaration under penalty of perjury of _____ dated September 19, 1988, he declared as follows in relevant part: He was a member of the California Horse Racing Board ("CHRB") in November of 1987, and was designated by the CHRB to act as a Special Master on November 20, 1987 to make a recommendation to the

CHRB regarding a dispute between _____ and _____. He conducted a hearing with those gentlemen. He concluded that there was no lease between those gentlemen in effect on November 20, 1987 regarding the horse or regarding which of them could use their "silks" in the race on November 21, 1987. He made that recommendation to the CHRB. Firestone had argued that a lease dated August 30, 1985 was then in effect.

The Lease Agreement dated August 30, 1985 was between _____ as lessor, and _____ as lessee. It expressly covered the period from August 30, 1985 through January 1, 1986 with an automatic renewal for one more year unless _____ gave timely notice not to renew. _____ leased his 50 percent interest in _____ for racing qualities only. _____ was granted full and complete control and direction of racing performance, including the right to have the horse raced in _____ name and colors except that when possible, both names "shall" be used jointly. _____ was entitled to keep the race awards, except cash. The "rent" was listed as _____, receiving 50 percent of race purses for the benefit of _____, _____ agreed to bear 50 percent of expenses, plus the risk of loss.

Pursuant to another Lease Agreement dated August 15, 1985, _____ as lessor, leased its part ownership rights in _____ for racing quality purposes to _____ for successive one-year periods until _____ was disposed of or otherwise retired from racing. _____ was granted full and complete control and direction of the racing performance, including the right to non-cash awards, but _____ was to accept purses for the benefit of _____ maintained risk of loss and its share of expenses.

For the race on November 21, 1987, the racing form of the Hollywood Park Fall Operating Company indicated that _____ was owned by _____, with _____ as trainer, and with the colors/silks left blank. The horse and jockey actually raced in the colors/silks of _____, acted as trainer. _____ was the personal trainer of petitioner's principal, _____ Another horse _____ owned by _____ raced under the name of _____ and _____ won the race. Hollywood Park Fall Operating Company allocated the winnings and income for Franchise Tax Board purposes as follows: 10 percent to petitioner, 15 percent to _____, 50 percent to _____, and 15 percent to the other partner.

In prior races, [redacted] had raced under the owner's name of "[redacted]", with [redacted] as trainer, and under petitioner's colors/silks. [redacted] personally had been invoiced for the charges to ship the horse to California on November 2, 1987.

On November 22, 1987, [redacted] issued a check for the additional \$350,000 purchase price to the escrow holder's trust account.

On November 24, 1987, the escrow holder commenced the searches by contacting the States of California, Illinois, Florida, Kentucky and Virginia for encumbrances. Apparently, none was found. In an invoice dated November 24, 1987, [redacted] billed [redacted] for \$11,342.47 interest due on the prepayment of "[redacted] installment note--November 23, 1987 (23 days @ 9% per annum)", and \$5,113.92 as "Full Mortality Insurance Premium for [redacted] at \$200,000 per share/per diem rate \$365.28 November 20 through December 4, 1987 (14 days x 365.28) (to be adjusted according to actual closing date)". [redacted] represented that this second charge was only for [redacted] 50 percent ownership share of insurance costs, which [redacted] paid.

[redacted] represented to me that trainer [redacted] had informed [redacted] that [redacted] had retained physical possession of the horse until November 28, 1987, including with two of his employees accompanying the horse on the shipment from California to [redacted] farm in Kentucky on November 27, 1987. [redacted] invoiced petitioner for training services for [redacted] through November 28, 1987. [redacted] further represented that all the co-owners paid their pro-rata shares of those charges, including petitioner for this 10 percent interest. [redacted] had been invoiced for the charges for the shipment of the horse from California to Kentucky on November 27, 1987.

On December 8, 1987, [redacted] signed The Jockey Club Certificate of Foreign Registration for the horse on his own behalf, as president of [redacted] and managing general partner of petitioner, in which [redacted] he represented that on that date, petitioner sold to [redacted] its 10 percent interest in [redacted]. [redacted] was listed as owner of a 15 percent interest in [redacted].

On December 9, 1987, the escrow holder delivered the bill of sale and certificate to [redacted], and the purchase price to petitioner. The contents of the bill of

sale include a provision that petitioner "does hereby sell, convey and transfer to [redacted] the 10 percent interest in the horse; and that petitioner had not previously hypothecated, pledged or encumbered any right, title or interest in that 10 percent interest.

A [redacted], signed under penalty of perjury a Declaration dated December 13, 1991, wherein he made the following pertinent representations: He had been associated with the escrow holder law firm in November 1987 and had been personally involved in the transaction. He had known of a serious dispute regarding a lease agreement and of a lack of trust between [redacted] and [redacted]. He had also been involved in the Agreement negotiations and drafting. He then acted on behalf of petitioner. At that time, [redacted] attorney, [redacted] would not recommend for [redacted] to proceed with the transaction without complete title/lien searches, given the substantial amount of money involved and the lack of trust then existing between the parties. He had insisted on the provision in the Agreement regarding the transfer of risk of loss in order to prevent [redacted] from avoiding the contract if the horse's value dropped as a result of the race. The Agreement provision regarding [redacted] acquisition of right to possession and control of the horse "was essentially a reflection of the status quo...." [redacted] had already been a co-owner in constructive co-possession of the horse. It had been previously agreed by the co-owners that the horse would come to California solely to run in the race under the possession and control of [redacted] for the benefit of all co-owners, with the understanding that it would then be delivered to [redacted] Kentucky farm for a career as a breeding stallion under [redacted] control for the account of all owners. [redacted] last check cleared his bank on November 30, 1987. That had been a requirement to the close of escrow. The registration certificate was placed into escrow on December 8, 1987, following a chain of title search. He is informed and believes that [redacted] made the final payment on the 1985 promissory note on December 8, 1987, including an \$11,342.47 interest payment. All the conditions of the sale were satisfied by December 9, 1987, and escrow was then closed.

The audit staff concluded that the sale occurred in California on November 20, 1987 when the agreement was executed because petitioner then completed its performance under that contract by having [redacted] accept physical possession and risk of loss, and by delivering a bill of sale to the escrow holder. Consideration was contended to consist of the check funds paid into escrow on November 20, 1987.

Regulation 1628(b)(3)(D) was cited as authority for that conclusion.

In a report dated December 10, 1991, one or more Board supervising auditors wrote about this case following a discussion with petitioner's representatives: They cited Revenue and Taxation Code section 6006 and Regulation 1628(b)(3)(D) as authority for a California sale because possession and control of, and risk of loss for, this horse transferred to [redacted] on November 20, 1987. It was further represented that [redacted] was then leasing [redacted] percent interest in the horse pursuant to a Lease Agreement dated August 30, 1985, and therefore petitioner and [redacted] had actual possession and control of the horse prior to the November 20, 1987 Agreement. Board annotation 395.1120 was cited as support for those conclusions since possession of the horse had been transferred with petitioner retaining title as security for payment of the purchase price. Annotations 395.1140 and 395.1160 were cited as involving different facts.

At the conference, Ms. Gerber and Mr. Smith presented the Department's case as follows: A California sale had occurred either on November 20, 1987 when risk of loss transferred or on November 22, 1987 when trainer took possession of the horse. Thereafter, petitioner had no possession or right to possession. [redacted] then used the horse in California until November 27, 1987 when it went to Kentucky. Although it is not known if title transferred, there was a transfer of possession in lieu of a transfer of title. The consideration consisted of [redacted] assumption of the risk of loss. The paperwork contingencies were not enough to prevent a transfer of ownership. [redacted] could have immediately validly conveyed this 10 percent interest to someone else. All the elements of annotation 395.1120 were met.

I asked Mr. Smith hypothetically if he would have paid [redacted] money prior to December 9, 1987 for this 10 percent interest in [redacted]. He said no for the following reasons: there were too many contingencies; escrow was still open; and he would have waited until the contingencies had occurred.

[redacted] indicated that he had represented throughout this time period. He represented that both parties had intended that the sale not occur until the contingencies were met.

At the conference, petitioner's representatives said, among other things, that the sale was not an

occasional sale because they understood that petitioner probably made multiple sales of horse interests around the time of this sale. Petitioner's counsel then and has since made multiple arguments on why no California sale occurred: (1) the parties explicitly agreed to a sale/transfer of title at a subsequent time, if any, when escrow would close after all contingencies were removed and the bill of sale, The Jockey Club Registration Certificate and purchase price were exchanged; (2) there was no actual transfer of possession to _____, in California; (3) if there was a California transfer of possession, it was not in lieu of a transfer of title, exchange or barter; (4) there was no transfer of title when the horse was located in California; (5) there was no actual, or even an opportunity for, reservation/retention of title in the horse by petitioner of any security interest; (6) there were legitimate business reasons (the contingencies) which had to take place while the agreement was still executory and before the sale occurred which did not actually take place until after the horse left California; (7) the California Horse Racing Board and The Jockey Club consider a horse sold only when The Jockey Club Registration Certificate is endorsed; (8) the parties still considered each other as an owner while escrow was open; (9) no valuable consideration existed until the close of escrow; (10) the transfer of risk of loss is not a sale; (11) the checks did not clear the bank until after the horse left California; (12) annotation 395.1120 is distinguishable since it involved the sale of a whole business, plus it is contradictory to annotation 395.1140; (13) the change in risk of loss is not consideration; (14) petitioner did not have exclusive possession of this horse prior to November 20, 1987 since the previous Lease Agreement was no longer valid; (15) _____ could not have sold the 10 percent interest in this horse to a third person prior to December 9, 1987; (16) _____ had only a contractual right which was available to be sold to a third party prior to December 9, 1987; (17) Regulation 1628 involves only transportation charge issues which is not in issue here; (18) under Commercial Code section 2401(1), title passes at the time and place explicitly agreed to by the contracting parties; and (19) title transferred when the bill of sale was delivered on December 9, 1987.

Analysis and Conclusions

Sales tax is imposed upon retailers measured by the gross receipts derived from California retail sales of tangible personal property (Revenue and Taxation Code sections 6003 and 6051). A "sale" is defined in Revenue and Taxation Code section 6006 as follows:

"(a) Any transfer of title or possession, exchange, or barter, conditional or otherwise, in any manner or by any means whatsoever, of tangible personal property for a consideration. 'Transfer of possession' includes only transactions found by the board to be in lieu of a transfer of title, exchange, or barter.

The place of sale is the place where the tangible personal property is physically located at the time the act constituting the sale takes place (Rev. & Tax. Code § 6010.9).

California Commercial Code section 2401 reads, in pertinent part, as follows:

"(1)...Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest. Subject to these provisions and to the provisions of the division on secured transactions (Division 9), title to goods passes from the seller to the buyer in any manner and on any conditions explicitly agreed on by the parties.

"(2) Unless otherwise explicitly agreed title passes to the buyer at the time and place at which the seller completes his performance with reference to the physical delivery of the goods, despite any reservation of a security interest and even though a document of title is to be delivered at a different time or place;

The Board's Regulation 1628(b) reads as follows in pertinent part:

"(3) DETERMINATION OF WHEN SALE OCCURS.

"(D) Other Sales. Unless explicitly agreed that title is to pass at a prior time, the sale occurs at the time and place at which the retailer completes his performance with reference to the physical delivery of the property, even though a document of title is to be delivered at a different time or place.

If the contract requires or authorizes the retailers to send the property to the purchaser but does not require him to deliver it at destination, the retailer completes his performance with reference to the physical delivery of the property at the time and place of shipment, e.g., delivery of the property to a carrier for delivery by the carrier to the purchaser; but if the contract expressly requires delivery at destination, including cases where one of the terms of the contract is F.O.B. place of destination, the retailer completes his performance with reference to the physical delivery of the property on tender to the purchaser there. When delivery of the property is by facilities of the retailer, title passes when the property is delivered to the purchaser at the destination unless there is an explicit written agreement executed prior to the delivery that title is to pass at some other time.

"(4) PLACE OF SALE. For the purposes of the State Sales and Use Tax Law (but not for the purposes of the Bradley-Burns Uniform Local Sales and Use Tax Law nor for the purposes of the Transactions and Use Tax Law) the place of the sale or purchase of tangible personal property is the place where the property is physically located at the time the act constituting the sale or purchase takes place."

The following constitutes the findings and conclusions of the Board's Appeals Review Section:

By express written agreement (paragraph 7.1) dated November 20, 1987, the parties transferred the exclusive rights to possession and control of this 10 percent interest in this horse from petitioner to [redacted] while the horse was located in the stables at the California race track. As a co-owner, [redacted] already had the right of possession and control to another 50 percent interest because the lease agreement with [redacted] s then no longer in effect. [redacted] had already been acting on behalf of [redacted]

regarding that 50 percent interest. As a result of the provisions of the November 20, 1987 agreement, _____ took delivery and obtained actual possession of the 10 percent interest on November 20, 1987 when the agreement was signed because _____ retained physical possession of the horse. On November 21, 1987 when the horse raced under personal colors rather than under petitioner's colors as in all prior races, _____ was in possession and control of the 10 percent interest. _____ was then acting on behalf of _____ as to the 10 percent interest. Petitioner had made the 10 percent interest available for _____ and _____ had taken actual physical possession through a person acting on his behalf, _____

The sale thus occurred in California prior to the horse leaving for Kentucky. Title, ownership, actual possession and the right to possession of this horse passed from petitioner to _____ in California on November 20, 1987. Thus, pursuant to Revenue and Taxation Code section 6006(a), a sale took place. Under Regulation 1628(b)(3)(D) and California Commercial Code section 2401(2), title passed and the sale occurred in California when petitioner completed its performance with reference to the physical delivery of the horse, despite a reservation of a security interest and even though documents of title were to be delivered at a later time. Although Regulation 1628 is labelled transportation charges, the Board uses subsection (b)(3)(D) as a general authority on an issue of when a sale occurs. The attempted retention or reservation by petitioner of title to the horse after the delivery to _____ as limited in effect to a reservation of a security interest (Calif. Com. Code § 2401(1)). Title passes only as explicitly agreed upon by the parties only when the Commercial Code does not provide otherwise (§ 2401(1)). In this case, the Commercial Code provides otherwise.

The consideration for the California sale consisted of _____ promise to pay petitioner for the 10 percent interest in the horse. A promise by a purchaser to pay the seller at a future date for property already received is consideration for Sales and Use Tax Law purposes (see Peterson Tractor Co. v. State Board of Equalization (1962) 199 Cal.App.2d 662, 670; and Civil Code § 1605).

The preponderance of the evidence shows that although the parties intended to delay the time of sale to a later time when all of the conditions were actually removed, they intended to immediately transfer possession and control of petitioner's interest in the horse. The

conditions were conditions subsequent rather than conditions precedent. An escrow itself does not prevent the sale from occurring. Pursuant to section 6006(a), the transfer of title or possession can be conditional. In addition to the contract provision regarding the transfer of the right to possession and control of the 10 percent interest in the horse, the parties also agreed to transfer the risk of loss to

This latter term also supports the conclusion that a sale occurred on November 20, 1987. The parties further agreed to the remedy of specific performance, which tends to support an immediate sale. The lack of a lien investigation or chain of title search did not make the 10 percent interest to be of non-conforming quality. The only interest of petitioner remaining thereafter was a security interest, notwithstanding any explicit agreement to the contrary. The reason that petitioner thereafter shared in the race proceeds was due to its contractual right rather than any benefit of its security interest still held. The phrase "current ownership percentages" in paragraph 7.1 of the contract merely referred to the percentages prior to signing the agreement.

There are no known legal authorities which would have restricted the sale of this 10 percent interest until the occurrence of any of the conditions, including the transfers of the bill of sale or registration certificate, or the clearance of the bank checks.

The above-mentioned Board annotations were pre-Commercial Code opinions and were thus decided under somewhat different law, including Revenue and Taxation Code section 6006(e). However, the conditions involved therein can be considered to distinguish those opinions and support the conclusions in this case. In the two annotations in which it was concluded that no sale had occurred (395.1140 [4/14/58] and 395.1160 [4/14/58]), respectively, critical factors existed: (1) In one, it was concluded that California law prohibited the transfer of title to the assets of the business which held an on-sale liquor license; and (2) in the other, possession of the tangible personal property was transferred to the expected purchaser pursuant to an oral rental agreement which was separate from the contract of sale. In the third case, in which it was opined that a sale had occurred at the time of the transfer of possession of the fixtures and equipment, there were no such factors or similar evidence which would have prevented a conclusion of a sale (395.1120 [7/30/58]). In our situation herein, there were no such or similar factors of the type which would preclude a

conclusion of a sale at the time and place of the transfer of possession of the property.

Revenue and Taxation Code section 6396 provides that there is a sales tax exemption when, pursuant to a contract of sale, the property is required to be shipped and it is actually shipped to a point outside California by the retailer either by means of facilities operated by the retailer or by delivery to a carrier for such shipment.

This authority does not provide for exemption in this case. The contract of sale between these two parties did not require the horse to be shipped to any out-of-state point. The available evidence indicates that there was a prior agreement between the parties that the horse would be shipped from California to ~~arm~~ in Kentucky. However, that agreement had nothing to do with any sale. No sale was then anticipated--petitioner then expected to remain an owner while the horse was thereafter retired from racing. When the November 20, 1987 sales agreement was reached, no shipment of the horse was contemplated as part of the sale terms. The sales agreement expressly provided that the right to possession and control of the 10 percent interest in the horse passed at the time that written agreement was signed on November 20, 1987. There was no need for any "shipment" by the seller as part of the sale. The interest in the horse was delivered by the seller to the purchaser in California. The purchaser was thereafter in a position to do whatever he desired with his 10 percent interest.

Petitioner should be relieved of the penalty since the failure to file a California use tax return was based upon the mistaken but reasonable belief that a Kentucky sale had occurred in reliance upon some of the language in the agreement.

Recommendation

It is the recommendation of the Appeals Review Section that the determination be redetermined without further adjustment, except for a deletion of the penalty.

Stephen A. Ryan
Stephen A. Ryan, Senior Staff Counsel

7-23-92
Date

JA