



STATE BOARD OF EQUALIZATION

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November 5, 1996

E. L. Sorensen, Jr.
Executive Director

Mr. W--- -. L---
A--- A--- ---
--- ---, Suite XXX
--- ---, California XXXXX-XXXX

Re: Account No. S- -- XX-XXXXXX

Dear W---:

This is in response to your October 2, 1996 letter to Assistant Chief Counsel Gary Jugum asking whether your client, J--- A---, Inc. (hereafter "J--- A---") qualifies as a "new trade or business" within the meaning of Revenue and Taxation Code section 6377(b)(5)(A)¹ and Title 18, California Code of Regulations (hereafter "Regulation"), section 1525.2.

You state:

"J--- A--- ... is currently constructing a compact disc manufacturing facility in --- ---, California. Construction on this facility began after January 1, 1994, and does not include the acquisition of any existing manufacturing facilities located outside California. However, neither J--- A--- [n]or any related party have owned or operated any manufacturing facilities within California within the last three years. J--- A--- has a sales office located in Los Angeles but only engages in sales solicitation from this office.

"J--- A--- and any related parties have not engaged in any activities in California which would be classified under Division D of the 1987 Standard Industrial Classification Manual within the past three years...."

¹ All further references are to the Revenue and Taxation Code unless otherwise noted.

For purposes of this request, you ask that we assume that J--- A--- qualifies for all other applicable provisions of the partial sales and use tax exemption. As such, our opinion below does not address whether J--- A--- actually qualifies for the partial sales and use tax exemption and instead only addresses whether your client qualifies as a “new trade or business.”

Discussion

The partial sales and use tax exemption is generally available to persons that commence a new trade or business (discussed below) on or after January 1, 1994 inside this state which is described in codes 2000 to 3999² of the 1987 Standard Industrial Classification Manual (hereafter "SIC code"). A new trade or business is one which a person (or any related person) has not engaged in within the preceding 36 months inside this state³ or which is classified in a different division of the SIC code than that person's (or any related person's) current or prior trade or business activities in this state. (Rev. & Tax. Code § 6377(b)(5)(A)(ii).)⁴ That is, a person must not be regarded as having engaged in a manufacturing activity inside this state within the 36 months preceding the time it actually engages in the new trade or business activity inside this state. The new trade or business must also commence its new operations inside this state on or after January 1, 1994. (Reg. 1525.2(c)(5)(A).) Generally, we regard business operations to begin upon the acquisition of operating assets that are necessary to the type of business contemplated. (See Reg. 1525.2(c)(5)(A)1.)

Under an earlier draft of Regulation 1525.2(c)(5)(A)3, a person was regarded as having conducted a manufacturing operation inside this state if it merely operated a warehouse or sales office inside this state for its out-of-state manufacturing operation. Language reflecting this position was not, however, adopted by the Board in the final version of Regulation 1525.2(c)(5)(A)3 and is not therefore a condition for qualifying as a new trade or business. Thus, a person is regarded as having undertaken a manufacturing operation in California only if it actually engaged in a business operation described in SIC codes 2000 to 3999 inside this state.

You state that J--- A--- has a sales office located in Los Angeles but that it only engages in sales solicitations from that office. We assume that these sales operations fall within the non-manufacturing SIC division F,⁵ “Wholesale trade” (durable and non-durable goods), involving the wholesale distribution of durable and non-durable goods. As such, J--- A---’s activities inside this state do not constitute a manufacturing operation previously undertaken inside this

² SB 38, among other things, amends the applicable SIC codes to 2011 through 3999. SB 38 was recently signed by the Governor and is effective January 1, 1997.

³ Section 6377 makes a distinction between persons engaged in a trade or business inside the state and those that are not. Persons engaged in business wholly outside the state who commence doing business in California on or after January 1, 1994 qualify as a new trade or business regardless of that person's prior trade or business activity. (See Rev. & Tax. Code § 6377(b)(5)(A)(iii).)

⁴ “New trade or business” status is further limited in situations where a person acquires the assets of another business. (See Rev. & Tax. Code § 6377(b)(5)(A)(i).) Since we understand that J--- A--- did not acquire the assets of another business inside California, we will not address the acquisition provisions of the partial sales and use tax exemption.

⁵ Division F contains SIC codes 5012 through 5199.

Mr. W--- -. L---

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state. This means that J--- A--- is not precluded from qualifying as a “new trade or business” based on its current and past sales operations inside this state.

If you have any further questions, please write again.

Sincerely,

Warren L. Astleford
Tax Counsel

WLA:rz

cc: San Francisco District Administrator - (BH)