

February 6, 1984

Mr.

Business Inventory Exemption – Production Modules

This is in response to your December 9, 1983 memorandum to Larry Augusta wherein you Enclosed copies of correspondence from the Alameda County Assessor's Office, an Agreement between Redacted (SAPC) and Redacted (SCC), and business inventory exemption Letters to Assessors and correspondence, and you inquired. concerning the availability of the business inventory exemption for oil production modules being constructed by SCC in Alameda, Contra Costa, and San Joaquin Counties for use in Alaska by SAPC and others pursuant to the Agreement.

As Letters to Assessors Nos. 75/83 010 and S0/69 D1.2 indicate, property held by a subsidiary corporation for sale to its parent corporation is eligible for the exemption:

“Assume that... company ...were to organize a subsidiary whose business was to sell spare parts to the parent company, Would the spare parts owned by the subsidiary qualify as business inventories?”

Answer: Yes”

The May 23, 1972 memorandum from Knowles to Mayer, the January 29, 1974 letter from Florence to Shellenberger, the June 13, 1975, letter from McManigal to Hutchinson, the September 23, 1975, memorandum from Knowles to Beeler, and the December 31, 1975, letter from Florence to Seeley are to the same effect. The rationale for such conclusion is set forth in May 23, 1972, memorandum and in the January 25, 1974, memorandum from Delaney to Florence attached to the January 29, 1974, letter: absent the lack of a legitimate business purpose, separate corporate entities must be recognized as such, even though they may be related entities, and such sales may be at cost or without an intent to make a profit.

The conclusions in the above in the above mentioned Letters to Assessors and correspondence have not changed.

Although it is indicated that SAPC is believed to be at all. times the owner of the modules because under Article 6.1 of the Agreement SAPC pays for all materials and labor ill advance and because there are no dollar amounts mentioned therein, the Agreement states, among other things, that SCC will provide engineering and design services with respect to the facilities, manufacture, fabricate, and sell the facilities to SAPC, and inspect, transport, install and test the facilities, together, the “Contract Activities” (Article 1.1); that in consideration for the Contract Activities undertaken, including the purchase price for the facilities manufactured, SAPC agrees to

compensate SCC in accordance with the provisions of Exhibit A (Article 4); and that any controversies or claims arising out of or relating to the Agreement shall be determined by California Law (Article 26). The Agreement is silent as to the time of passage of title to the facilities/modules.

Given the manufacture and sale of modules, Article 5.1 merely authorizing advance payments for costs of material and labor, and I given the applicability of California Law, California Commercial Code Section 2401(2) provides with respect to passage of title:

"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, ... and in particular and despite any reservation of a security interest by the bill of lading

“(b) If the contract requires delivery at destination, title passes on tender there.”

And, while neither Agreement nor Exhibit A mentions specific dollar amounts to be paid for the modules and services undertaken by SCC, Article 4 and Exhibit A do provide for the computation of the compensation to be paid SCC. Such are acceptable payment provisions in light of California Commercial Code -Section 2J05(1), which provides that parties may conclude a contract. for sale even though the price is not settled, if they so intend.

Finally, although it is indicated that SCC is believed to be acting only as an agent for SAPC, not as a seller of modules, per CAL. Jur. Ill, Agency S1, an agent is one who represents another , called the principal, in dealings with third persons; the contract creating the relation of principal and agent is called a contract of agency; and the right of the agent to act on behalf of his principal is termed his authority or power. Further, the essential characteristics of an agency relationship are that an agent holds power to a power to alter legal relations between both the principal. and the agent itself, that an agent is a fiduciary with respect to matters within the scope of the agency, and that a principal has a right to control the conduct of the agent with respect to matters entrusted to it.

Review of the Agreement discloses the absence of such characteristics: no contract of agency, no reference to principal and agent relationship, no authorization permitting SCC to represent SAPC in dealings with third persons or to alter legal relations between SAPC and itself or others, and no right of SCC to control the conduct of SCC. Rather, the Agreement states that SCC will provide engineering and design services with respect to the facilities, manufacture, fabricate and sell the facilities to SAPC, and inspect, transport, install and test the facilities, together, the “Contract Activities” (Article 1.1); and that SCC is an independent contractor with

Mr.

February 6, 1984

the right to supervise, manage, and control the performance of the details of the Contract Activities, SAPC being interested only in the results of the same (Article 21).

An independent contractor is one who, while rendering service in the course of an independent employment or occupation, must follow his employer's desires only as to the results of the work, and not as the means whereby it is to be accomplished (3 cal. Jur. 111 Agency 5 3). Such right to control the manner and means of accomplishing the desired result is the most important factor in distinguishing agent from an independent contractor (3 Cal. Jur. 111 Agency S 3).

JKM:fr

cc: Mr. Lawrence A. Augusta
Mr. Gordon P. Adelman
Mr. Robert H. Gustafson
Mr. Charlie Knudsen
Legal Section