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Richard W. Craigo
Craigo & Zimmermann

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Sales and Use Tax Planning for the Horse Industry

BY RICHARD W. CRAIGO*

The great majority of U.S. racing and major breeding jurisdictions have a system of sales and use taxes. Rather than address the statutory provisions on a state by state basis, this Article presents an overview of the many uniform aspects of these state sales and use tax laws, and explores how different jurisdictions approach those types of potentially taxable transactions that are most common to the horse industry. Substantial planning opportunities exist for the legitimate avoidance of these forms of taxation, as will be noted throughout this Article.

I. AN OVERVIEW OF STATE SALES AND USE TAXATION

The thirty-four states with legalized horse racing are surprisingly uniform in their general approach to sales and use taxation. The great majority employ both these forms of taxation; at last count, the exceptions were Montana, New Hampshire, Oregon, and Delaware. Virtually every state with a sales tax also employs a complementary use tax.

The basic sales tax is generally applicable to retail sales, which most states define as sales for any purpose other than resale in the ordinary course of business. The general theory of the resale exception is that the tax should apply only when the ultimate consumer acquires the property. Sales tax rates vary among the states from 3% to 8.25% of retail sales prices.¹

Sales taxes generally apply only to sales of tangible personal property. Thus, sales of stocks, bonds, or other intangible rights, and compensation paid for personal services are generally not taxed. Virtually all states have closed the loophole that would result

* Partner in the law firm of Craig & Zimmermann, Los Angeles, California. B.A. 1956, University of Arkansas; J.D. 1966, University of Southern California; California Certified Tax Specialist.

¹ ABA SALES & USE TAX HANDBOOK § 33-000 (1988) (in New York, combined state and local tax can total 8.25%); COLO. REV. STAT. § 39-26-106 (1982) (state sales tax is 3%).

if it were possible to avoid the sales tax by leasing tangible personal property instead of purchasing it. Accordingly, most states apply the tax to the leasing of tangible personal property.

Another potential loophole that sales tax jurisdictions have dealt is the situation where tangible personal property is purchased outside the taxing state, with the intention of bringing it into the taxing state for "storage, use or other consumption"² there. This is where the use tax becomes operative, generally covering (almost always at the sales tax rate) all property purchased out-of-state and thereafter brought into the taxing state if the sale of such property would have been subject to the sales tax had the purchase and sale occurred within the taxing state. The nature of potential sales and use tax transactions are so different that sales and use taxes will never apply to the same transaction. Thus, the two taxes are said to be complementary.

There are some differences between the states in their expressed rationale for the sales tax. Most states, including California, specify that it is a tax on the "privilege" of making retail sales.³ Other states, notably New York, denote it as a "destination" tax⁴ and still others apply a "gross receipts" test.⁵ Despite the differing rationales, the practical results are generally the same.

The seller generally is responsible for collecting the sales tax from the purchaser. Conversely, it is the purchaser who generally is responsible for payment of use tax on transactions involving out-of-state purchases followed by importation to the taxing state, except in cases where the retailer selling the property outside the taxing state also does business within the taxing state. In that case, the seller may be primarily responsible for collection.

All states have exempted or excluded various categories of tangible personal property from the scheme of taxation. This Article will limit the discussion of these exemptions and exclusions to equine assets. All states also exempt or exclude certain types of purchase and sale transactions, as hereafter discussed.

A. Interstate and Foreign Sales

The commerce clause of the United States Constitution⁶ has been interpreted as prohibiting any state tax that discriminates

² CAL. REV. & TAX. CODE § 6201 (West 1987).

³ See, e.g., CAL. REV. & TAX. CODE § 6051.

⁴ ABA SALES & USE TAX HANDBOOK § 33-220 (1988).

⁵ ABA SALES & USE TAX HANDBOOK § 18-113.01 (1988) (Kentucky).

⁶ U.S. CONST. art. I, § 8, cl. 3.

against interstate commerce.⁷ Likewise, the import-export clause of the Constitution⁸ generally prohibits taxation by any state of goods that are to be exported from the United States.⁹ Recognizing this, most states specifically exempt from the tax sales for export from the taxing state. However, the statutes are often rigid and must be strictly complied with if taxation is to be avoided. For example, most states still attempt to tax sales of property destined for interstate shipment or foreign export if (a) the purchaser takes possession of the property within the taxing state or even arranges for shipment of the property, or (b) any use is made of the purchased property prior to its delivery outside the taxing state.¹⁰

B. Occasional Sales

Many states recognize the inequity of designating every sale of tangible personal property as a retail sale even though made to ultimate consumers. Thus, a number of states have exempted sales by one who is not a typical retailer.¹¹ Again, however, the exemption is limited to situations where such sales are few in number or of inconsequential amount. For example, in both Kentucky and California, one generally is considered a retailer if more than two sales of tangible personal property are made within any twelve-month period.¹² Since typical race horse owners and breeders (with the exception of market breeders) do not consider themselves to be in a retail business, the occasional sale provisions of the various jurisdictions are of paramount importance to the horse industry and are discussed hereafter in connection with sales of horses.

C. Commercial Exemptions

Most states exempt certain commercial transactions where no change in the beneficial ownership of tangible personal property occurs, such as transfers of property to owned partnerships or corporations and distributions of property on the liquidation of such entities. These exemptions must be analyzed carefully. For example, California exempts a sale of tangible personal property

⁷ See generally *Western Livestock v. Bureau of Revenue*, 303 U.S. 250 (1938).

⁸ U.S. CONST. art. I, § 10, cl. 2.

⁹ See *Peck & Co., Inc. v. Lowe*, 247 U.S. 165 (1918).

¹⁰ Title 18 *California Code of Regulations*, Reg. 1620(b)(3).

¹¹ See *infra* notes 63-67 and accompanying text.

¹² KY. REV. STAT. ANN. § 139.110(1)(c) (Michie/Bobbs-Merrill 1982) [hereinafter K.R.S.]; CAL. REV. & TAX. CODE § 6019 (West 1987).

by a closely-held corporation to a shareholder, but only if the sale is to a shareholder owning more than eighty percent of the corporate stock and only if more than eighty percent of the corporation's tangible personal property is sold in that transaction.¹³

D. Administration

Each state, of course, has a governmental agency administering the sales and use tax laws. Each state also has specific rules and regulations regarding the requirements for filing returns, for audits, for proceedings to collect alleged tax deficiencies, for taxpayers' rights to appeal adverse decisions and for applicable statutes of limitation on the state's assertion of tax deficiencies. In general, the taxing state requires a taxpayer to file appropriate sales or use tax returns and specifies a period of limitations, generally three or four years, on the time allowed for the state to assess taxes and penalties. Where no return is filed, there is usually no time limit on assessment. California is an exception, having an eight-year statute of limitations when no return is filed.¹⁴ As to the taxpayer's court of last resort, the almost-universal rule is that if the taxing authority turns down all avenues of taxpayer appeal, then the taxpayer may seek relief in the civil courts. However, this appeal may come at a price. For example, in California, the tax, penalties, and interest must be paid before having access to the civil courts.¹⁵

The efficacy of any tax depends heavily on the resources that the taxing state is willing to allocate to the taxing authority. In recent years, both Kentucky and California have made a concerted effort to increase this type of revenue collection, especially in the equine industry. The result has been a vast increase in the taxation of equine transactions. Owners and breeders, at least in those two jurisdictions, cannot afford to be complacent about these forms of taxation. Unless they know the rules of the game, the chances of sales and use tax liability are substantial.

II. SPECIFIC EQUINE-RELATED ISSUES

A. Sales Tax

In general, in-state sales of horses are subject to sales tax unless they constitute sales for resale or qualify as "occasional sales" in

¹³ CAL. REV. & TAX. CODE § 6006.5(a)-(b) (West 1987); Title 18 *California Code of Regulations*, Reg. 1595(b)(2).

¹⁴ CAL. REV. & TAX. CODE § 6487.

¹⁵ CAL. REV. & TAX. CODE § 6931.

jurisdictions that offer that relief.¹⁶ However, there are numerous exceptions to the general rule of taxation. The following are some of the different categories of sales tax treatment by the various states.

Sales of horses are generally exempt from any sales tax in Alabama, Arizona, Connecticut, South Carolina, Texas, Vermont, Washington, and Wyoming.¹⁷ Louisiana exempts public sales of horses sponsored by a breeders or registry association.¹⁸

Sales of horses used for breeding purposes generally are exempt from sales tax in Colorado, Florida, Georgia, Illinois, Kentucky, Maryland, Michigan, New York, and Ohio.¹⁹ In Idaho, the exempt sale must be in connection with the operation of a farm for profit.²⁰ In Oklahoma, sales by a person engaged in the business of raising horses for market are exempt.²¹ In Virginia, sales to a farmer-horse breeder are exempt.²²

Kentucky requires that in order to be exempt from sales tax, the horse being sold must be used for "breeding purposes only."²³ Accordingly, any use for racing after purchase would defeat the exemption. However, there are situations where the purchase and sale of a substantial stallion prospect is desirable shortly before the end of its racing career. The question is whether such a sale can be bifurcated in order to take advantage of the breeding exemption.

For example, assume that a stallion prospect is to be retired immediately after the Breeders' Cup to be held at Churchill Downs, but that on the eve of the race a \$1 million offer, acceptable to the owner, is received. The offer is contingent upon the horse racing in the name and silks of the purchaser. Since the horse is

¹⁶ *Id.*

¹⁷ ALA. CODE § 40-23-4(a)(5) (Michie Supp. 1989); ARIZ. REV. STAT. ANN. § 42-1310-.01 (C)(5) (1989); CONN. GEN. STAT. ANN. § 12-412(12)(F) (West Supp. 1989); S.C. CODE ANN. § 12-35-550(3) (Law. Co-op. 1976); TEX. TAX CODE ANN. § 151.316(1) (Vernon Supp. 1989); VT. STAT. ANN. tit. 32, § 9741(3) (1981); WASH. REV. CODE ANN. § 82.08.0259 (1987); WYO. STAT. § 39-6-505(a)(ix) (1985).

¹⁸ LA. REV. STAT. ANN. § 47:305A(2) (West Supp. 1989).

¹⁹ COLO. REV. STAT. § 39-26-114(5) (1982); FLA. STAT. ANN. § 212.07(7) (West 1989); GA. CODE ANN. § 48-8-5 (1982); ILL. ANN. STAT. ch. 120, para. 441, § 2,(a-1) (Smith Hurd 1989); K.R.S. § 139.531(2)(a) (1982); MD. TAX.-GEN. CODE ANN. § 11-201(1) (1988); MICH. COMP. LAWS § 205.54a(f) (Supp. 1989); N.Y. TAX LAW § 1115(a)(6) (McKinney 1987); OHIO REV. CODE ANN. § 5739.02(17) (Page Supp. 1988).

²⁰ IDAHO CODE § 63-3622D (1989).

²¹ OKLA. STAT. ANN. tit. 68, § 1358(B) (West Supp. 1989).

²² VA. CODE ANN. § 58.1-608.2a (1989).

²³ K.R.S. § 139.531(2)(a) (1982).

training at Churchill Downs, it is not practical to move it from the state prior to the race. Can the parties avoid all or a portion of the potential Kentucky sales tax that will otherwise apply?

Avoidance may be possible. Suppose that the owner leases the racing qualities of the horse to the purchaser for \$100,000 for a term ending shortly after the Breeders' Cup race (so that the horse will race in the name and silks of the purchaser as lessee). Suppose, further, that the parties agree to grant options to each other, the purchaser having an option to purchase the horse for an additional \$900,000 and the seller having an option to force the purchaser to complete the purchase after the race for the additional \$900,000. If title is deemed to pass only after the race, then the \$900,000 may be exempt from sales tax. There would be an even better chance of success if the parties negotiate a spread between the buyer's option and the seller's option. For example, the purchaser might have an option to purchase after the race for \$900,000, and if not exercised, then the seller might have the right to exercise the second option after the race, to cause the purchaser to complete the purchase for \$875,000. Under such circumstances, it is possible that neither option will be exercised. Accordingly, the actual sale should not be considered as occurring until after the final race when one of the options is actually exercised. In that event, the sales price should be exempt from Kentucky sales tax under the "breeding purposes only" exemption.

Horses sold by the in-state producer (generally the breeder) are exempt from sales tax in New Mexico,²⁴ in Louisiana and Florida (if sold by the breeder),²⁵ and in Arkansas and Oklahoma (if the sale is by private treaty or at a special livestock sale).²⁶ Minnesota exempts sales of horses conceived and born in that state.²⁷

B. Stallion Shares, Seasons, and Lifetime Breedings

There is a wide divergence between major breeding states in the treatment of sales of stallion shares and seasons. The sale of syndicated fractional interests ("shares") in breeding stallions probably is exempt from the sales tax in the same states that exempt

²⁴ N.M. STAT. ANN. 7-9-18 (1988).

²⁵ LA. REV. STAT. ANN. § 47:305 A.(1) (West Supp. 1989); FLA. STAT. ANN. § 212.07(5) (West 1989).

²⁶ ARK. STAT. ANN. § 26-52-401(18)(F)(ii) (Supp. 1989); OKLA. STAT. ANN. tit. 68, § 1358(B) (West Supp. 1989).

²⁷ MINN. STAT. ANN. §§ 297A.01 subd. 13 (Supp. 1990), 297A.25 subd. 1(h) (1972).

the sale of all horses or the sale of breeding horses, most notably Florida, Illinois, Kentucky, Maryland, New York, Ohio, Texas, Vermont, and Washington since it is reasonable to consider the sale of a percentage interest in a horse the same as the sale of the entire horse.²⁸ On the other hand, such sales are generally taxable elsewhere.

In the typical stallion syndication, up to forty shares are sold, usually to different purchasers. Even where not specifically exempted, a seller might claim that the shares are intangible property in the nature of an interest in a partnership, or could claim that application of an "occasional sale" exemption should apply, since a single horse is involved. However, in most jurisdictions, the taxing authority will consider such sales of stallion shares to be sales of tangible personal property (undivided interests in the stallion) and will find that the sale of multiple shares to different purchasers constitutes a number of separate sales, thus eliminating any "occasional sale" consideration.²⁹

The treatment of the sale of an annual stallion breeding season also differs among major breeding states. Such sales are treated as sales of tangible personal property (usually argued to be the semen) in some states, the prime example being Kentucky.³⁰ Conversely, such sales are either specifically exempt, or are exempt as sales of *intangible* personal property (a decidedly more logical view) in others.³¹ Although the sale of seasons is taxable in Kentucky, an exchange of such seasons is not.³² However, any cash boot paid in the exchange would presumably be taxable.

Of current interest, especially in Kentucky, is the recent decision reached in the Pillar Stud dispute³³ dealing with the question of who may be held responsible for collection of the tax on sales of breeding seasons. In that case, Kentucky attempted to hold the

²⁸ FLA. STAT. ANN. § 212.07(7) (West 1989); ILL. ANN. STAT. ch. 120, para. 441, § 2 (Smith-Hurd Supp. 1989); K.R.S. § 139.531(2)(a) (1982); MD. TAX-GEN. CODE ANN. § 11-201a(1) (1988); N.Y. TAX LAW § 1115(a)(6) (McKinney 1987); OHIO REV. CODE ANN. § 5739.02(17) (Page Supp. 1988); TEX. TAX CODE ANN. § 151.316(1) (Vernon Supp. 1989); VT. STAT. ANN. tit. 32, § 9741(3) (1981); WASH. REV. CODE ANN. § 82.08.0259 (1987).

²⁹ CAL. REV. & TAX. CODE § 6006.5 (West 1987); California State Board of Equalization, Ruling 540.0280.

³⁰ See K.R.S. § 139.531(2)(b) (1982).

³¹ E.g., Virginia specifically exempts breeding fees from sales tax. VA. CODE ANN. § 58.1-608.2(a) (1989).

³² K.R.S. § 139.531(2)(b) (1982).

³³ Pillar Stud, Inc. v. Kentucky Revenue Cabinet, File No. K88-R-26, Order No. K-12933 (B.T.A. 1989).

syndicate manager (in this case, Pillar Stud, Inc.) of the stallion responsible for collecting the tax, even though its only involvement may have been the receipt of a communication that the season had been transferred, followed by the new transferee being allowed to breed to the stallion. The Kentucky Board of Tax Appeals rejected this position and held that stallion managers were not responsible for collection of sales tax on transfers of breeding seasons by other stallion share owners where the stallion manager is neither the owner, transferor, transferee, seller, sales agent, purchaser nor user of the breeding season.³⁴ The Board reasoned that if agents of retailers (here the stallion managers) were liable in this context, then clerks in any retail store would likewise be liable for sales tax.³⁵

Should a sale of a right to annually breed to a given stallion for his entire breeding life be treated as the sale of a share, or as the sale of a series of annual breeding rights? The answer will have substantial tax consequences. If the stallion is syndicated, it can be forcefully argued that a lifetime breeding right has the same primary right as the share, namely the right to breed a mare annually. The fact that it is a nonvoting right, as usually is the case, might be seen as incidental to the primary right. Accordingly, a lifetime breeding right could be treated as an ownership interest and thus a sale of tangible personal property (exempt, for example, under the Kentucky breeding exemptions, but taxable under California law).

A current case involving Calumet Farm and the stallion Alydar addresses this issue.³⁶ Kentucky claimed that the sale of a lifetime breeding right is taxable, presumably as the sale of a series of taxable breeding seasons. The taxpayer claimed that such a sale is tantamount to the sale of an ownership interest in the stallion and is thus exempt as the sale of a breeding animal. In this case, Alydar is not a syndicated stallion, but the case did not turn on that fact. Moreover, in this case the holders of the lifetime breeding rights have priority rights to breed. This fact lends even stronger support to the position that the lifetime breeding right is an ownership interest. Nevertheless, the court held that the sale of the lifetime

³⁴ *Id.* at 2 (citing *Barnes v. Department of Revenue*, 575 S.W.2d 169 (Ky. App. 1978)).

³⁵ *Id.* at 3.

³⁶ *Calumet Farm, Inc. v. Kentucky Revenue Cabinet*, No. 87CI-3435 (Div. 1, Fayette Cir. Ct., Civ. 1989).

breeding right was a taxable sale as the holders did not have an ownership interest in the horse.³⁷

C. Auction Sales

In Louisiana, a public sale of livestock sponsored by a breeders or registry association is exempt from tax.³⁸ In most other jurisdictions, auction sales of horses are taxable except when the purchase is for the purpose of resale or is for shipment outside the taxing state. "Buy-backs"³⁹ are generally not taxed. As previously noted, care must be taken with the interstate commerce exemption rules. For example, California requires that at the time of the auction sale a contract must exist requiring the seller to deliver the horse, or causing a common carrier to deliver the horse, to the purchaser outside of California.⁴⁰ If the purchaser takes possession in California or if the purchaser alone arranges for shipment of the horse, then the interstate commerce or foreign export exemptions may not apply. Whether the requirement that a contract to ship out-of-state must exist at the time of an auction sale (fall of the hammer) has been met may ultimately depend on the content of written statements found in the sales catalogue, the auctioneer announcements prior to sale, and signs posted by the auction company.

D. Sales of Race Horses

Sales tax liability is the general rule for sales of race horses. The same is true of leasing race horses. Florida exempts sales of race horses by their breeders.⁴¹ Minnesota exempts the sale of any horse conceived and born there.⁴² Of course, the general rules exempting sales for resale, occasional sales, and sales in interstate or foreign commerce apply equally to sales of race horses. Kentucky has a special interstate commerce rule, exempting purchases by nonresidents of horses under two years of age (which may be deemed January 1 by the state, instead of applying chronological age) if the horse is purchased for shipment outside of Kentucky

³⁷ *Id.*

³⁸ LA. REV. STAT. ANN. § 47:305A.(2) (West Supp. 1989).

³⁹ A "buy-back" is where the seller is the successful bidder.

⁴⁰ CAL. REV. & TAX. CODE § 6396 (West 1987).

⁴¹ FLA. STAT. ANN. § 212.07(5) (West 1989).

⁴² MINN. STAT. ANN. § 297A.01 subd. 13 (Supp. 1990), § 297A.25 subd. 1(h) (1972).

for racing or showing, even though the horse temporarily remains in Kentucky to be trained for racing or showing.⁴³

"Claims" of horses generally are subject to sales tax, being exempt from tax only in Louisiana.⁴⁴ New York has a progressive rule, taxing only that portion of the claiming price in excess of the highest prior claiming price paid for the horse during the same year.⁴⁵ This rule recognizes the inequity of a full tax on each of several claims that might occur during a given year.

E. Use Tax

Purchases of horses out-of-state, followed by importation into the taxing state, subject the horse to use tax in most jurisdictions, unless substantial use occurs subsequent to purchase and prior to importation, or unless an occasional sale rule applies to such a purchase in a given jurisdiction. However, there are important exceptions to the general rule. Purchase and importation of horses generally are exempt from use tax in Connecticut, Idaho (if for "agricultural" use), Illinois (only as to breeding stock), Kentucky (if brought into Kentucky exclusively for breeding purposes), New York (only as to race horse value in excess of \$100,000), Tennessee, Texas, Vermont, Virginia, and Washington.⁴⁶

Given the now commonplace movement of horses between states, it is highly advisable for each owner and trainer, with regard to recently purchased horses, to understand the interaction of the laws in the various states that apply use taxes. For example, assume that Owner A, a nonresident, purchases a yearling race horse prospect late in the year in Kentucky, where it is exempt from sales tax under the special Kentucky interstate commerce rule discussed above.⁴⁷ May Owner A safely transport the horse to California to train for its first race (both training and racing constitute a "use" in virtually all jurisdictions) without incurring use tax liability?

⁴³ K.R.S. § 139.531(2)(c) (1982).

⁴⁴ LA. REV. STAT. ANN. § 47:305A.(2) (West Supp. 1989).

⁴⁵ N.Y. TAX LAW § 1111(g) (Consol. 1988).

⁴⁶ CONN. GEN. STAT. ANN. § 12-412(12)(F) (West Supp. 1989); IDAHO CODE § 63-3622D (1989); ILL. ANN. REV. STAT. ch. 120, para. 439.3, § 3 (Smith-Hurd 1989); K.R.S. § 139.531(2)(a) (1982); N.Y. TAX LAW § 1118(10) (McKinney 1987); TENN. CODE ANN. § 67-6-301(b) (1989); TEX. TAX CODE ANN. § 151.316(1) (Vernon Supp. 1989); VT. STAT. ANN. tit. 32, § 9741(3) (1981); VA. CODE ANN. § 58.1-608.2(a), (c) (Supp. 1989); WASH. REV. CODE ANN. § 82.12.0261 (1987).

⁴⁷ See *supra* note 43 and accompanying text.

In California, applicability of use tax depends upon a variety of factors, including a) the length of time between the out-of-state purchase of the horse and its importation into California; b) the extent of the use of the horse in California (in the case of race horses, more than a single race);⁴⁸ c) the extent of subsequent use of the horse outside California; and d) the residence of the owner.⁴⁹

A horse purchased and raced outside California in more than one complete race meet will not be subject to use tax if subsequently imported to California.⁵⁰ However, if "first use" occurs in California, the tax generally will apply, as it will to any use in California unless first used outside of California for a substantial period prior to importation.⁵¹ There is a presumption that all property is purchased for use in California⁵² unless the property remains and is used outside California for more than ninety days after purchase.⁵³ Thus, the safest method to avoid California use tax is to use the horse outside California for over ninety days before importation.

An excellent planning opportunity may exist for purchases by California residents of Kentucky yearlings. On the one hand, as previously noted, Kentucky sales of horses under two years of age are exempt if the horse is purchased for use outside Kentucky, even though temporarily trained in Kentucky after such sale. On the other hand, training is a "use" that, if continuing for over ninety days outside California, should exempt the horse from California use tax upon importation to California. Thus, a simple but effective plan for a California resident purchasing Kentucky yearlings may be to have such yearlings trained for more than ninety days in Kentucky, and only thereafter imported to California. The potential sales and use taxes of both states thus could be avoided.

In Kentucky, breeding stock of both sexes brought into the state for breeding purposes only are exempt from use tax.⁵⁴ Accordingly, it may be prudent planning for out-of-state purchasers of breeding stock to have such stock immediately shipped to Kentucky for breeding in at least the initial year of ownership. Pre-

⁴⁸ CAL. REV. & TAX. CODE § 6202 (West 1987); *Sales Tax Counsel* 9-1-53.

⁴⁹ CAL. REV. & TAX. CODE § 6247 (West 1987).

⁵⁰ Title 18 *California Code of Regulations*, Reg. 1620(b)(3).

⁵¹ CAL. REV. & TAX. CODE § 6202; *Sales Tax Counsel* 3-27-51.

⁵² CAL. REV. & TAX. CODE § 6246.

⁵³ Title 18 *California Code of Regulations*, Reg. 1620(b)(3); *Sales Tax Counsel* 1-21-

⁵⁴ K.R.S. § 139.531(2)(a) (1982).

sumably the purchase would be exempt from sales tax by the state of purchase as a sale in interstate commerce, exempt from use tax in Kentucky under the breeding purposes exemption, and thereafter likely exempt from use tax in the state of ultimate destination since the first subsequent use will have been made in another state, viz., Kentucky.⁵⁵

In Florida, there is a presumption against applicability of the use tax if the property is used outside Florida for at least six months after purchase and before importation.⁵⁶ In Maryland, temporary importation by nonresidents for the purpose of racing is exempt from use tax. However, if the horse remains in Maryland for over thirty days, it will be presumed to be permanently located in Maryland and will be subject to use tax.⁵⁷ Kentucky also exempts from use tax horses brought into the state for "temporary use" for racing.⁵⁸ In New Jersey, use tax does not apply to race horses purchased and imported by a nonresident, provided such nonresident has not commenced substantial activity relating to racing in New Jersey.⁵⁹

In New York, use tax applies if a race horse is entered in more than five races during the calendar year.⁶⁰ If used outside New York for more than six months after purchase, New York use tax will be based on fair market value at the time of the first in-state use (rather than basing the tax on the purchase price).⁶¹ However, even if a race horse is subject to New York use tax, the value of the horse in excess of \$100,000 is exempt from tax.⁶²

F. Horses and the Occasional Sale Rule

The occasional sale rule presents the greatest opportunity for tax avoidance by the average horse owner and breeder. This discussion will concentrate on the almost identical Kentucky⁶³ and

⁵⁵ *Id.*

⁵⁶ FLA. STAT. ANN. § 212.06(8) (West 1989).

⁵⁷ MD. TAX-GEN. CODE ANN. § 11-214(2) (1988).

⁵⁸ K.R.S. § 139.531(3) (1982).

⁵⁹ N.J. STAT. ANN. § 54:32B:11(2) (West 1986).

⁶⁰ N.Y. TAX LAW § 1118(9) (McKinney 1987).

⁶¹ N.Y. TAX LAW § 1111(b)(1).

⁶² N.Y. TAX LAW § 1118(10).

⁶³ K.R.S. § 139.110(1)(c) (1982): "(1) Retailer includes: (c) Every person making more than two (2) retail sales during any twelve (12) month period, including sales made in the capacity of assignee for the benefit of creditors, or receiver or trustee in bankruptcy."

California⁶⁴ rules, which consider those persons who make more than two retail sales within a twelve month period to be retailers. The comments may also apply to other jurisdictions with similar rules.

When a selling horse owner attempts to establish that he or she is an occasional seller as to a particular transaction under the rule regarding two retail sales, certain sales may not "count" against the owner. For example, California auctioneers (as to auction sales of horses) and race tracks (as to claiming races) are designated by statute as the retailers responsible for collection of the sales tax on these transactions.⁶⁵ Accordingly, it has been ruled that such sales are not to be treated as sales by the taxpayer and therefore cannot "count" against the taxpayer for purposes of the occasional sale rule.⁶⁶ On the other hand, even though a horse is sold out-of-state, and is exempt from tax under the interstate commerce exemption, it may nevertheless be treated as a "retail sale" and thus "count" against the taxpayer for purposes of applicability of the occasional sale rule.⁶⁷

As to use taxes and occasional sale rules, the use tax generally applies only when the transaction would have been subject to sales tax had it occurred in the taxing state. Accordingly, it is logical to apply the occasional sale rule to test out-of-state purchases for purposes of determining use tax liability. California has recognized this reasoning.⁶⁸ The task for the practitioner in such states is to demonstrate that the out-of-state seller was in fact making an occasional sale to the importing purchaser-taxpayer. This may be accomplished by obtaining affidavits or declarations from the sellers to that effect.

CONCLUSION

In the major racing and breeding states, virtually every purchase and sale, lease, or syndication of a horse, an interest in a

⁶⁴ CAL. REV. & TAX CODE § 6019 (West 1987):

Every individual, firm, copartnership, joint venture, trust, business trust, syndicate, association or corporation making more than two retail sales of tangible personal property during any 12-month period, including sales made in the capacity of assignee for the benefit of creditors, or receiver or trustee in bankruptcy, shall be considered a retailer within the provisions of this part in his or its individual, firm, copartnership, joint venture, trust, business trust, syndicate, associate or corporate capacity.

⁶⁵ CAL. REV. & TAX CODE §§ 6015, 6019 (West 1987).

⁶⁶ *Id.* at § 6019; *Sales Tax Counsel* 6-10-53.

⁶⁷ CAL. REV. & TAX CODE §§ 6015, 6019; *Sales Tax Counsel*, 10-21-52.

⁶⁸ *Sales Tax Counsel* 8-11-52, 10-21-52.

horse, or a breeding right has possible sales and use tax implications. Moreover, in several major states, including California and Kentucky, these taxing statutes are being applied with vigor. Accordingly, the purchaser and seller should always inquire, before any purchase or sale, as to whether the transaction will be subject to such forms of taxation. If so, consideration should be given to the substantial planning opportunities for legitimate avoidance of these taxes.