



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

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October 17, 2008

To Interested Parties:

**Notice of Proposed Regulatory Action
by the
State Board of Equalization**

Proposed to Adopt Regulation 1705, *Relief from Liability*

NOTICE IS HEREBY GIVEN

The State Board of Equalization, pursuant to the authority vested in it by section 15606(a) of the Government Code, proposes regulatory changes to Sales and Use Tax Regulation 1705, *Relief from Liability*, in Title 18, Division 2, Chapter 4, of the California Code of Regulations, relating to sales and use tax. A public hearing on the proposed regulation amendments will be held in Room 121, 450 N Street, Sacramento, at 9:30a.m., or as soon thereafter as the matter may be heard, on Tuesday, December 16, 2008. At the hearing, any person interested may present statements or arguments orally or in writing relevant to the proposed regulatory action. The Board will consider written statements or arguments if received by December 16, 2008.

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

CURRENT LAW: Revenue and Taxation Code section (Section) 6596 provides relief from tax, interest, and penalty charges due on a transaction if the Board determines that the taxpayer failed to pay tax because it reasonably relied on erroneous written advice from the Board. For relief to apply, the Board must have received a written request for advice on the transaction, the request must have identified the taxpayer to whom the advice applied, and the request must have fully described the facts and circumstances of the transaction. Section 6596 subdivision (d) states that, “[o]nly the person making the written request shall be entitled to rely on the board’s written advice to that person.” Accordingly, taxpayers cannot obtain relief by relying on a written opinion given to another business, even if the transactions are similar. However, a taxpayer may rely on advice given to the taxpayer’s representative provided that the representative identifies the person for whom the advice is requested. Regulation 1705, *Relief from Liability*, is based upon Section 6596 and explains its provisions in more detail. In 1999, Regulation 1705 was amended to extend Section 6596 relief to trade or industry association members when an association requests written advice on behalf of its members. In order to obtain relief under Section 6596, the members must be identified in the association’s request for advice. Proposed

regulatory changes to Regulation 1705, explain that similar relief applies to franchisees and franchisors.

COST TO LOCAL AGENCIES AND SCHOOL DISTRICTS

The State Board of Equalization has determined that the proposed regulation does not impose a mandate on local agencies or school districts. Further, the Board has determined that the proposed regulation will result in no direct or indirect cost or savings to any State agency, any local agency or school district that is required to be reimbursed under Part 7 (commencing with section 17500) of Division 4 of Title 2 of the Government Code, or other non-discretionary cost or savings imposed on local agencies, or cost or savings in Federal funding to the State of California.

EFFECT ON BUSINESS

Pursuant to Government Code section 11346.5(a)(7), the Board of Equalization makes an initial determination that the proposed regulatory changes to Sales and Use Tax Regulation 1705 will have no significant statewide adverse economic impact directly affecting business.

The adoption of the proposed regulation will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

The regulation as proposed will not be detrimental to California businesses in competing with businesses in other states.

The proposed regulation may affect small business.

COST IMPACT ON PRIVATE PERSONS OR BUSINESSES

The Board is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

SIGNIFICANT EFFECT ON HOUSING COSTS

No significant effect.

FEDERAL REGULATIONS

Proposed Regulation 1705 has no comparable federal regulations.

AUTHORITY

Section 7051, Revenue and Taxation Code.

REFERENCE

Section 6596, Revenue and Taxation Code

CONTACT

Questions regarding the substance of the proposed regulation should be directed to Ms. Lisa Andrews (916) 322-5989, at 450 N Street, Sacramento, CA 95814, e-mail Lisa.Andrews@boe.ca.gov or by mail at State Board of Equalization, Attn: Lisa Andrews, MIC:50, P.O. Box 942879, 450 N Street, Sacramento, CA 94279-0050.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, telephone (916) 445-2130, fax (916) 324-3984, e-mail Richard.Bennion@boe.ca.gov or by mail at State Board of Equalization, Attn: Rick Bennion MIC:81, P.O. Box 942879, 450 N Street, Sacramento, CA 94279-0080.

ALTERNATIVES CONSIDERED

The Board must determine that no reasonable alternative considered by it or that has been otherwise identified and brought to its attention would be more effective in carrying out the purpose for which this action is proposed, or be as effective as and less burdensome to affected private persons than the proposed action.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared an initial statement of reasons and an underscored version (express terms) of the proposed regulation. Both of these documents and all information on which the proposal is based are available to the public upon request. The Rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed regulation are available on the Internet at the Board's web site <http://www.boe.ca.gov>.

AVAILABILITY OF FINAL STATEMENT OF REASONS

The final statement of reasons will be made available on the Internet at the Board's web site following its public hearing of the proposed regulation. It is also available for your inspection at 450 N Street, Sacramento, California.

ADDITIONAL COMMENTS

Following the hearing, the State Board of Equalization may in accordance with law adopt the proposed regulation if the text remains substantially the same as described in the text originally made available to the public. If the State Board of Equalization makes modifications which are substantially related to the originally proposed text, the Board will make the modified text, with the changes clearly indicated, available to the public for fifteen days before adoption of the regulation. The text of any modified regulation will be mailed to those interested parties who

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commented on the proposed regulatory action orally or in writing or who asked to be informed of such changes. The modified regulation will be available to the public from Mr. Bennion. The State Board of Equalization will consider written comments on the modified regulation for fifteen days after the date on which the modified regulation is made available to the public.

Sincerely,

A handwritten signature in cursive script that reads "Diane G. Olson".

Diane G. Olson, Chief
Board Proceedings Division

DGO:reb

Enclosures

**Initial Statement of Reasons
Overview/Non-Controlling Summary**

PROPOSED REGULATION 1705, RELIEF *from Liability*,

Proposed Regulation 1705 is proposed to be revised to explain when a franchisee is relieved from the liability to pay tax based on erroneous written advice provided to its franchisor?

Specific Purpose

The purpose of the proposed regulation is to interpret, implement, and make specific Revenue and Taxation Code section 7261. This regulation is necessary to provide guidance to taxpayers affected by this statute.

Factual Basis

Revenue and Taxation Code section (Section) 6596 provides relief from tax, interest, and penalty charges due on a transaction if the Board determines that the taxpayer failed to pay tax because it reasonably relied on erroneous written advice from the Board. For relief to apply, the Board must have received a written request for advice on the transaction, the request must have identified the taxpayer to whom the advice applied, and the request must have fully described the facts and circumstances of the transaction. Section 6596 subdivision (d) states that, “[o]nly the person making the written request shall be entitled to rely on the board’s written advice to that person.” Accordingly, taxpayers cannot obtain relief by relying on a written opinion given to another business, even if the transactions are similar. However, a taxpayer may rely on advice given to the taxpayer’s representative provided that the representative identifies the person for whom the advice is requested. Regulation 1705, *Relief from Liability*, is based upon Section 6596 and explains its provisions in more detail. In 1999, Regulation 1705 was amended to extend Section 6596 relief to trade or industry association members when an association requests written advice on behalf of its members. In order to obtain relief under Section 6596, the members must be identified in the association’s request for advice. Proposed regulatory changes to sales and use tax regulation 1705, *will* explain that similar relief applies to franchisees and franchisors.

Pursuant to Government Code section 11346.5(a)(8), the Board of Equalization finds that the adoption of the proposed regulation will not have a significant adverse economic impact on private businesses or persons. The regulation is proposed to interpret, implement, and make specific the authorizing statutes. These changes will clarify the interpretation or administration of the sales and use tax laws. Therefore, the Board has determined that these changes will not have a significant adverse economic impact on private businesses or persons.

Proposed amendments to Regulation 1705

Regulation 1705. RELIEF FROM LIABILITY.

Reference: Section 6596, Revenue and Taxation Code.

(a) IN GENERAL. A person may be relieved from the liability for the payment of sales and use taxes, including any penalties and interest added to those taxes, when that liability resulted from the failure to make a timely return or a payment and such failure was found by the Board to be due to reasonable reliance on:

- (1) Written advice given by the Board under the conditions set forth in subdivision (b) below; or
- (2) Written advice in the form of an annotation or legal ruling of counsel under the conditions set forth in subdivision (d) below; or
- (3) Written advice given by the Board in a prior audit of that person under the conditions set forth in subdivision (c) below. As used in this regulation, the term "prior audit" means any audit conducted prior to the current examination where the issue in question was examined.

Written advice from the Board may only be relied upon by the person to whom it was originally issued or a legal or statutory successor to that person. Written advice from the Board which was received during a prior audit of the person under the conditions set forth in subdivision (c) below, may be relied upon by the person audited or by a legal or statutory successor to that person.

The term "written advice" includes advice that was incorrect at the time it was issued as well as advice that was correct at the time it was issued, but, subsequent to issuance, was invalidated by a change in statutory or constitutional law, by a change in Board regulations, or by a final decision of a court of competent jurisdiction. Prior written advice may not be relied upon subsequent to: (1) the effective date of a change in statutory or constitutional law and Board regulations or the date of a final decision of a court of competent jurisdiction regardless that the Board did not provide notice of such action; or (2) the person receiving a subsequent writing notifying the person that the advice was not valid at the time it was issued or was subsequently rendered invalid. As generally used in this regulation, the term "written advice" includes both written advice provided in a written communication under subdivision (b) below and written advice provided in a prior audit of the person under subdivision (c) below.

(b) ADVICE PROVIDED IN A WRITTEN COMMUNICATION.

(1) Advice from the Board provided to the person in a written communication must have been in response to a specific written inquiry from the person seeking relief from liability, or from his or her representative. To be considered a specific written inquiry for purposes of this regulation, representatives must identify the specific person for whom the advice is requested. Such inquiry must have set forth and fully described the facts and circumstances of the activity or transactions for which the advice was requested.

(2) A person may write to the Board and propose a use tax reporting methodology for qualified purchases subject to use tax. If the Board concludes that the reporting method reflects the person's use tax liability for the defined population, then the Board may write to the person approving the use of the reporting method. The approval shall be subject to certain conditions. The following conditions shall be included in the approval:

- (A) The defined population of the purchases that will be included in the reporting method;
- (B) The percentage of purchases of the defined population that is subject to tax;
- (C) The length of time the writing shall remain in effect;
- (D) The definition of a significant or material change that will require rescinding the approved reporting method; and
- (E) Other conditions as required.

The written approval of the use tax reporting methodology is void and shall not be relied upon for the purposes of Revenue and Taxation Code section 6596 if the taxpayer files a claim for refund for tax that had been reported based upon this reporting method.

(c) WRITTEN ADVICE PROVIDED IN A PRIOR AUDIT. Presentation of the person's books and records for examination by an auditor shall be deemed to be a written request for the audit report. If a prior audit report of the person requesting relief contains written evidence which demonstrates that the issue in question was examined, either in a sample or census (actual) review, such evidence will be considered "written advice from the Board" for purposes of this regulation. A census (actual) review, as opposed to a sample review, involves examination of 100% of the person's transactions pertaining to the issue in question. For written advice contained in a prior audit of the person to apply to the person's activity or transaction in question, the facts and conditions relating to the activity or transaction must not have changed from those which occurred during the period of operation in the prior audit. Audit

Proposed amendments to Regulation 1705

comments, schedules, and other writings prepared by the Board that become part of the audit work papers which reflect that the activity or transaction in question was properly reported and no amount was due are sufficient for a finding for relief from liability, unless it can be shown that the person seeking relief knew such advice was erroneous.

(d) ANNOTATIONS AND LEGAL RULINGS OF COUNSEL. Advice from the Board provided to the person in the form of an annotation or legal ruling of counsel shall constitute written advice only if:

(1) The underlying legal ruling of counsel involving the fact pattern at issue is addressed to the person or to his or her representative under the conditions set forth in subdivision (b) above; or

(2) The annotation or legal ruling of counsel is provided to the person or his or her representative by the Board within the body of a written communication and involves the same fact pattern as that presented in the subject annotation or legal ruling of counsel.

(e) TRADE OR INDUSTRY ASSOCIATIONS OR FRANCHISORS. A trade or industry association requesting advice on behalf of its member(s) must identify and include the specific member name(s) for whom the advice is requested for relief from liability under this regulation. A franchisor requesting advice on behalf of its franchisee(s) must identify and include the specific franchisee name(s) for whom the advice is requested for relief from liability under this regulation.

For an identified trade or industry member or franchisee to receive relief based on advice provided in the written communication to the trade or industry association or franchisor, the activity or transactions in question must involve the same facts and circumstances as those presented in the written inquiry by the association or franchisor.

Regulation History

Type of Regulation: Sales and Use Tax

Regulation: 1705

Title: *Relief from Liability*

Preparation: Lynn Whitaker

Legal Contact: Christine Bisauta

Amendments are proposed to be adopted to clarify when a franchisee is relieved from sales or use tax liability based on erroneous advice provided to its franchisor.

History of Proposed Regulation:

September 16, 2008 BTC, Board Authorized Publication (Vote 5-0)
July 17, 2008 Second IP meeting
May 16, 2008 Last day for IP to respond to Initial Discussion Paper
April 29, 2008 First Interested Parties (IP) meeting

Sponsor: NA
Support: NA
Oppose: NA