

CALIFORNIA STATE BOARD OF EQUALIZATION

APPEALS DIVISION SUMMARY FOR BOARD HEARING

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3 In the Matter of the Petition for Reallocation)
4 of Local Tax Under the Uniform Local Sales)
5 and Use Tax Law of:)
6 CITY OF POMONA & TOWN OF LOS GATOS) Case ID 469261
7 Petitioners)

8 Retailer: Seller of data communication products

9 Date of knowledge: June 17, 1994 (Pomona)
September 28, 1994 (Los Gatos)

10 Allocation period:¹ July 1, 1993 – December 31, 2007 (Pomona)
October 1, 1993 – December 31, 2007 (Los Gatos)

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12 Estimated amount in dispute:² \$9,539,000³ (Pomona)
\$146,630⁴ (Los Gatos)

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14 Notifications required:⁵ Cities of Alhambra, Arcadia, Beverly Hills, Burbank, Carson,
15 Cerritos, Commerce, Covina, Culver City, Downey, El Monte, El
16 Segundo, Gardena, Glendale, Glendora, Hawthorne, Industry,
17 Inglewood, Lakewood, La Mirada, Lancaster, Long Beach, Los
18 Angeles, Manhattan Beach, Monrovia, Montebello, Norwalk,
19 Paramount, Pasadena, Redondo Beach, San Jose, Santa Clarita,
20 Santa Fe Springs, Santa Monica, Signal Hill, South Gate,

21 ¹ The allocation period ends on December 31, 2007, based on the date the Department operationally documented that the
22 taxpayer was misallocating the local tax. For the local tax for periods on and after January 1, 2008, the Department will be
23 reallocating the local sales tax mis-allocated to the countywide pool without regard to the present appeal, and will instruct
24 the taxpayer accordingly.

25 ² We are recommending granting most of the petitioned amounts in Pomona (for periods on and after October 1, 1993) and
26 all petitioned amounts in Los Gatos. However, notified jurisdictions have submitted briefs in connection with this hearing
27 to dispute our recommendation, and we therefore regard the entire petitioned amounts as in dispute.

28 ³ The Department calculates that the local tax distributed through the Los Angeles countywide pool during the reallocation
period for sales by the retailer delivered to California consumers from the Pomona location totals \$9,657,000. The
Department estimates that petitioner already received about \$118,000 as its share of that distribution (the actual
redistribution, if any, will be calculated based on the relative ratios distributed from the countywide pool to the participating
jurisdictions for the quarter prior to the quarter the redistribution is effected). Thus, if petitioner were to prevail on all
issues, the Department estimates the net redistribution to petitioner would be \$9,539,000. If, instead, our recommendation
is upheld to grant most, but not all, of the petitioned amounts, the Department estimates the net redistribution to petitioner
would be \$9,410,000.

⁴ The Department calculates that the local tax distributed through the Santa Clara countywide pool during the reallocation
period for sales delivered to California consumers from the Los Gatos location totals \$150,784. The Department estimates
that petitioner already received about \$4,154 as its share of that distribution. Thus, if our recommendation to grant the
petition were upheld, the Department estimates the net redistribution to petitioner would be \$146,630.

⁵ Pursuant to California Code of Regulations, title 18, section 1807, subdivision (d)(2).

1 Torrance, West Covina, West Hollywood, and Whittier, the
2 Palmdale Redevelopment Agency, and the County of Los
3 Angeles

4 BACKGROUND

5 The petitions in this appeal were filed on June 17, 1994, and September 28, 1994. An appeals
6 conference was held by the Local Tax Appeals Auditor within the Sales and Use Tax Department
7 (Department), and his Decision and Recommendation denying the appeal, issued on September 21,
8 1999, found that the retailer's warehouses in Pomona and Los Gatos were not places of sale that
9 required seller's permits. Petitioners timely appealed that decision to Board Management, who issued
10 its decision denying the appeal on July 24, 2000. On December 17, 2008, the Board granted
11 petitioners' request for hearing. On June 30, 2009, we prepared an Appeals Division Analysis
12 recommending that the petitions be granted as to local tax incurred for the periods beginning October
13 1, 1993, based on the warehouse making the delivery, and denied as to local tax incurred for the
14 periods prior to October 1, 1993, as explained below. The discussion under "Unresolved Issue" and
15 "Resolved Issue" summarize our recommendation as explained in our June 30, 2009 analysis. The
16 discussion under "Other Developments" addresses arguments raised in briefs filed in this appeal by
17 notified jurisdictions.

18 UNRESOLVED ISSUE

19 **Issue:** Whether the warehouse rule as explained in California Code of Regulations, title 18,
20 section (Regulation) 1802, subdivision (c), applies prior to October 1, 1993. We conclude that the
21 operative date which was added to Regulation 1802, subdivision (b)(5), in 1993 continues to apply,
22 and that the warehouse rule thus does not apply to periods prior to October 1, 1993 .

23 On November 15, 2005, the Board adopted amendments to Regulation 1699 and 1802 which
24 became effective December 13, 2006. Regulation 1699 now requires a permit for a location
25 maintaining a stock of goods (even if not the retailer's only location in California) which delivers such
26 goods pursuant to sales negotiated outside California. (Cal. Code Regs., tit. 18, § 1699, subd. (a).)
27 Regulation 1802 now provides for allocation of the local sales tax to the location maintaining a stock
28 of goods that makes the delivery if the sale was negotiated outside California and no other California
location of the retailer participated in the sale. (Cal. Code Regs., tit. 18, § 1802, subd. (c)(2.) Taken

1 together, these amendments provide for direct allocation of local sales tax to the jurisdiction of the
2 warehouse making the delivery to the California customer of retail sales negotiated outside California,
3 provided there is no participation by any other California location of the retailer.

4 Former subdivision (b)(5) (now subdivision (c)(1)) was added to Regulation 1802 by
5 amendment in 1993, with an operative date of October 1, 1993. When this provision was relettered as
6 subdivision (c)(1) in 2005, the October 1, 1993 operative date was deleted as no longer necessary. The
7 1993 amendment to Regulation 1802 provided that, *beginning October 1, 1993*, local tax would be
8 allocated to the local jurisdiction where a warehouse was located, if the retailer did not have a
9 permanent place of business in California other than a stock of goods. While the 2005 amendment
10 broadened the “warehouse rule” to apply to transactions by more retailers, there was no intent to
11 retroactively extend it farther back than the original October 1, 1993 operative date, despite the
12 deletion of that date in the 2005 amendment. Rather, the operative date was omitted simply because
13 the passage of time seemed to render it unnecessary. We find that the operative date of the warehouse
14 rule remains October 1, 1993, and that no reallocation is warranted for local sales tax incurred prior to
15 that date. Accordingly, we recommend that the petition of Pomona be denied as to local tax incurred
16 for periods prior to October 1, 1993.

17 **RESOLVED ISSUE**

18 We find that the local sales tax incurred on and after October 1, 1993, should be directly
19 allocated to petitioners based on the warehouse making the delivery to the California customer where
20 the sales were negotiated outside California and there was no participation by any California location
21 of the retailer other than the delivering warehouse. (This issue is resolved as between the Department
22 and petitioners, but is disputed by some notified jurisdictions, as discussed in the next section.)

23 **OTHER DEVELOPMENTS**

24 The HdL Companies (HdL), representing 23 affected jurisdictions,⁶ filed an opening brief
25 disputing Pomona’s position and our recommendation. The law firm of Richards, Watson & Gershon
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27 ⁶ The Cities of Alhambra, Arcadia, Burbank, Carson, Commerce, Covina, Culver City, Glendale, Glendora, Industry,
28 Inglewood, Lakewood, Lancaster, Monrovia, Montebello, Paramount, Redondo Beach, Santa Monica, Signal Hill, South
Gate, West Covina, West Hollywood, and Whittier.

1 (RWG), representing seven jurisdictions,⁷ filed a reply brief also disputing Pomona’s position and our
2 recommendation. MuniServices, LLC (MS), representing Pomona, filed a reply brief to HdL’s
3 opening brief and a response brief to RWG’s reply brief. Significant issues raised in these briefs are
4 identified below, along with our response.

5 Before we discuss the issues raised by notified jurisdictions, we first address a statement made
6 by MS on page 2 of its reply brief, which characterizes the Appeals Division as having found “that this
7 petition is valid back to October 1, 1993, and could have been granted within a reasonable time of its
8 filing in 1994.” This is a clear mischaracterization of our findings. We in no way stated that the
9 petition could have been granted “within a reasonable time of its filing in 1994.” In fact, we find that it
10 could not have been granted until the regulatory amendments effective on December 13, 2006, because
11 they operated retroactively. Granting the petition as to Pomona depends on whether the retailer’s
12 location in Pomona was required to hold a seller’s permit. In the summary prepared for the Board’s
13 consideration of the request for hearing, we stated:

14 “[A]t the time the D&R was issued and Board Management denied the appeal, there
15 was no basis for reallocating the local sales tax directly to the locations of the
16 unpermitted warehouses. (*Accord* former Cal. Code Regs., tit. 18, § 1802, subd.
17 (b)(5), the then applicable “warehouse rule” providing for direct allocation of local sales
18 tax to the jurisdiction in which the warehouse was located *if* the retailer had no
19 permanent place of business in this state other than the warehouse.) Instead, the tax had
20 been properly allocated through the pools of the counties of the respective warehouse
21 locations.”

22 The summary continued on to explain that, because of the adoption of amendments to Regulations
23 1699 and 1802 effective on December 13, 2006, we *retroactively* regard the Pomona warehouse
24 location as having required a seller’s permit. The analysis we prepared after the Board granted the
25 hearing similarly makes clear that “[a]t the time the petitions were filed, the D&R issued, and Board
26 Management denied the appeal,” a seller’s permit was not required for the Pomona warehouse of the
27 retailer. That is, the petition could *not* have been granted “within a reasonable time of its filing in
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⁷ The Palmdale Redevelopment Agency, and the Cities of Beverly Hills, Hawthorne, La Mirada, Pasadena, Norwalk, and South El Monte. We note that the Palmdale Redevelopment Agency and the City of El Monte were notified as substantially affected jurisdictions, but the Cities of Palmdale and South El Monte are not substantially notified jurisdictions and were not notified, and thus are not parties to this appeal. (Cal. Code Regs., tit. 18, § 1807, subd. (d)(3).)

1 1994,” and we never indicated that it could have been. Rather, it could not have been granted until the
2 effective date of the regulatory amendments, December 13, 2006, and can be granted for periods prior
3 to that date only because those amendments were not limited to prospective application.

4 Similar to the misstatement noted above, MS states on page 13 of its reply brief that our June
5 30, 2009 analysis and our summary prepared for the Board’s consideration of the request for hearing
6 “rejects the D&R analysis of these petitions.” As explained above, we absolutely did not, *and do not*,
7 reject the analysis of the D&R. Instead, the retroactive application of the amendments effective on
8 December 13, 2006, *retroactively* leave the analysis of the D&R behind. Now, on to the issues raised
9 by notified jurisdictions.

10 HdL and RWG contend that any reallocation is barred because Pomona’s request for Board
11 hearing was not filed within a reasonable period of time. In response, MS repeats the argument it
12 made in connection with its request for hearing that it diligently pursued correction of the
13 misallocation and that there was never any period that this appeal lay dormant. When the Board
14 considered Pomona’s request for hearing, the Appeals Division recommended that the hearing be
15 denied because the appeal was already closed. We explained our view that, under Pomona’s argument
16 regarding the guidelines in effect prior to the original adoption of Regulation 1807, a denial by Board
17 Management would never have been regarded as truly final, and we concluded this was an
18 unreasonable interpretation. However, the Board rejected our recommendation and granted the
19 hearing, which we understand as a finding that the matter does indeed remain open. As such, the
20 appeal is open and not barred by Revenue and Taxation Code section 7209, the applicable statute of
21 limitations. We note, however, that section 7209 is permissive only and does not require reallocation
22 (“The board may redistribute ...”), as discussed further below.

23 HdL states that MS did not have a valid resolution of Pomona (as required by Revenue and
24 Taxation Code section 7056 for MS to access confidential taxpayer information on Pomona’s behalf)
25 on file with the Board at the time MS requested the Board hearing in this matter. HdL further states
26 that the contract between MS and Pomona had also expired before MS requested the hearing. Based
27 on these facts, HdL contends that MS should have been precluded from making the request for hearing
28 on behalf of Pomona. Section 7056, subdivision (a)(1), establishes the Board’s duty to protect the

1 confidentiality of the business affairs, operations, or other non-public information pertaining to any
2 retailer or other person required to report or pay sales or use tax to the Board. Subdivision (b) provides
3 a method by which the Board may permit a person acting on behalf of a local jurisdiction to examine a
4 taxpayer's confidential records that pertain to that jurisdiction's local tax. Subdivision (b) does not,
5 however, include any prohibition against a person's representation of a local jurisdiction. That is, a
6 person chosen by a jurisdiction to represent it can do so even if that person does not satisfy the
7 requirements of section 7056, subdivision (b). Of course, such a representative will not have access to
8 confidential information (and will not be allowed to participate in confidential proceedings, such as an
9 appeals conference), and thus may well be hampered by that restriction in fully representing the
10 jurisdiction, but that is a matter between the jurisdiction and its chosen representative. Thus, without
11 regard to whether MS was authorized to access confidential information at the time it made the request
12 for Board hearing, we find that section 7056, subdivision (b), did not prohibit Pomona from retaining
13 MS as its representative to make the request for Board hearing.

14 MS requested a hearing in this matter on Pomona's behalf by letter to Board Member Leonard
15 dated September 9, 2008, which reflects copies were sent to Pomona City Manager Linda Lowry,
16 Pomona City Attorney Arnold Alvarez-Glasman, and Pomona Assistant City Attorney Andrew Jared.
17 Thus, we find that Pomona was aware that MS believed it was still Pomona's representative in this
18 matter, and Pomona at no time advised us that such was not the case. In fact, on June 1, 2009, Pomona
19 adopted a resolution stating that MS was, and continues to be, its representative in this matter.
20 Accordingly, we do not believe that appeal should be rejected based on this argument of HdL.

21 RWG claims that the 2005 amendments were not intended to, and cannot have, a retroactive
22 effect, and thus contends that the conclusion of the Decision and Recommendation should be upheld.
23 RWG cites various authorities for its position that the regulation is presumed prospective only, and that
24 it can apply retroactively only if expressly stating retroactive intent. RWG fails, however, to identify
25 and consider the authority that is actually directly on point, Revenue and Taxation Code section 7051:

26 "The board shall enforce the provisions of this part and may prescribe, adopt, and
27 enforce rules and regulations relating to the administration and enforcement of this part.
28 The board may prescribe the extent to which any ruling or regulation shall be applied
without retroactive effect."

1 This means that when the Board wishes to limit the retroactive effect of a regulation, it must
2 affirmatively state that the regulation is prospective only. (See *La Societe Francaise v. Cal. Emp.*
3 *Com.* (1943) 56 Cal.App.2d 534, 550.) Where the Board adopts a regulation without limiting its
4 retroactivity, then it is retroactive. For example, the warehouse rule was added to Regulation 1802 by
5 amendment in 1993 as subdivision (b)(5) (now subdivision (c)(1)) with an operative date of October 1,
6 1993. This is the reason the warehouse rule does not apply prior to that date (see discussion above),
7 and *not* the reverse as argued by RWG (which would be that the amendment was silent on
8 retroactivity, which is was not). There are a number of other examples of regulatory amendments
9 where the Board has expressly limited the retroactive effect of the amendment, and where it has not
10 done so, we interpret the regulatory change as fully retroactive (to the enabling provision, so if a
11 regulation was amended today to interpret a statute operative on January 1, 2004, the regulation would
12 be fully retroactive back to January 1, 2004, or, e.g., in the case of the 2006 change to the warehouse
13 rule, fully retroactive to the October 1, 1993 operative date of the enabling regulation for that rule). A
14 retroactive change applies to any matter that is still open. Here, the relevant regulatory amendments
15 were not made prospective only, and contain no operative dates or other language suggesting that the
16 amendments should operate prospective only. Thus, they were fully retroactive back to October 1,
17 1993, and apply in these appeals back to October 1, 1993, if, as we understand the Board to have held,
18 these appeals remain open.

19 RWG asserts that applying these changes retroactively under the facts here would constitute an
20 unconstitutional taking of its clients' funds, and that the Board is estopped from reallocating the
21 subject funds. We disagree. Had jurisdictions sought to limit the time for which a reallocation could
22 be made in the context of a lengthy appeals process, that could have been discussed in the interested
23 parties meetings concerning amendments to Regulation 1807, adopted by the Board last year, or when
24 Regulation 1807 was first adopted in 2002. As far as we recall, no one proposed such a limitation
25 during the discussions leading to the amendment of Regulation 1807 last year. Rather, our
26 understanding is that jurisdictions throughout California have consistently sought, to the maximum
27 extent possible, to reallocate funds to reflect the correct allocation of tax, knowing that doing so could
28 result in increases or decreases to their revenue, but always with the underlying goal of allocating the

1 correct amount of local tax to each jurisdiction. Furthermore, every jurisdiction has had the
2 opportunity to discuss these very types of issues during interested parties meetings concerning
3 proposed amendments to the local sales and use tax regulations, and then during the Business Tax
4 Committee meetings that follow, and again during the hearing on the adoption of any proposed
5 regulation. In sum, we believe that the process for resolving local tax disputes is very well understood
6 by the jurisdictions that have contracted with the Board to collect their local taxes, and they have been
7 given every opportunity to air their disputes regarding the procedures used to resolve these disputes.
8 We find no basis for finding there have been any due process violations, or for finding that reallocating
9 as we recommend would constitute an unconstitutional taking, or that the Board is estopped from
10 ordering such reallocation.

11 That being said, as noted above, even if the Board agrees that our recommendation correctly
12 applies the applicable regulations, if it were to find that the facts here justify a different result, it has
13 the discretion to reallocate a lesser amount than we recommend, including no reallocation at all. HdL
14 claims that any reallocation would cause a significant financial hardship to numerous jurisdictions and
15 is inappropriate, unnecessary, and unfair given the appeal was denied under the regulations applicable
16 at that time and only revived after these regulations were changed. Assuming the Board finds that the
17 appeal remains open, that the changes to the regulations are properly retroactive back to October 1,
18 1993, and that the changes authorize reallocation to Pomona, it still has the discretion to also find that
19 such reallocation should not be made because of the significant financial hardship to the numerous
20 jurisdictions or other reasons stated by HdL. However, barring such a finding, we recommend that the
21 local sales tax incurred on and after October 1, 1993, be directly allocated to petitioners, and that
22 Pomona's petition as to the local tax incurred prior to October 1, 1993, be denied.

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24 Summary prepared by Trecia M. Nienow, Tax Counsel III (Specialist)
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