STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-80
916-445-2130 • FAX 916-324-3984
www.boe.ca.gov

BETTY T. YEE
First District, San Francisco

SEN. GEORGE RUNNER (RET.)
Second District, Lancaster

MICHELLE STEEL
Third District, Rolling Hills Estates

JEROME E. HORTON
Fourth District, Los Angeles

JOHN CHIANG
State Controller

CYNTHIA BRIDGES
Executive Director

February 7, 2014

To Interested Parties:

Notice of Proposed Regulatory Action

The State Board of Equalization Proposes to Adopt Amendments to California Code of Regulations, Title 18, Section 1699, *Permits*

NOTICE IS HEREBY GIVEN

The State Board of Equalization (Board), pursuant to the authority vested in it by Revenue and Taxation Code (RTC) section 7051, proposes to adopt amendments to California Code of Regulations, title 18, section (Regulation) 1699, *Permits*, which incorporate and implement, interpret, and make specific RTC section 6070.5's provisions granting the Board authority to refuse to issue seller's permits to persons with outstanding final liabilities and non-natural persons controlled by persons with outstanding final liabilities. The proposed amendments add new subdivision (g) to Regulation 1699 and renumber the regulation's current subdivisions (g) through (j), as subdivisions (h) through (k), respectively. The proposed amendments also added a reference to RTC section 6070.5 to Regulation 1699's reference note.

PUBLIC HEARING

The Board will conduct a meeting in the Auditorium Room, at the California Public Utilities Commission's headquarters, located at 505 Van Ness Avenue, San Francisco, California, on March 25, 2014. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at *www.boe.ca.gov* at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on March 25, 2014. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1699.

AUTHORITY

RTC section 7051

REFERENCE

RTC sections 6066, 6067, 6070, 6070.5, 6071.1, 6072, 6073, 6075, and 6225

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

Current Law

In general, the Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.) requires every person desiring to engage in or conduct business as a seller of tangible personal property in California to apply to the Board for a seller's permit. (Rev. & Tax. Code, §§ 6014, 6066.) Under RTC section 6070, if a person fails to comply with any provision of the Sales and Use Tax Law, such as failure to remit payment of taxes, the Board can take action to revoke the person's seller's permit. This section also states that, after a person's seller's permit is revoked, the Board shall not issue a new permit to that person until it is satisfied the person will comply with the law.

RTC section 6070.5, as enacted by Assembly Bill No. (AB) 1307 (Stats. 2011, ch. 734), authorizes the Board to refuse to issue or revoke a seller's permit under certain conditions. Prior to the enactment of RTC section 6070.5, the Board did not have express statutory authority to refuse to issue a seller's permit to a person desiring to engage in the business of selling tangible personal property in California, unless the Board had previously revoked the person's seller's permit under RTC section 6070. And, the Board sponsored the enactment of RTC section 6070.5 to "provide additional tools that would assist the [Board] in reducing its growing outstanding accounts receivable balances from [the] failure to remit the taxes that are owed . . . ." (September 9, 2011, Assembly Floor Analysis of AB 1307.)

Currently, RTC section 6070.5, subdivision (a), provides that the Board may refuse to issue a permit to any person submitting an application for a seller's permit as required under RTC section 6066 if the person desiring to engage in or conduct business as a seller in California has an outstanding final liability for any amount due under the Sales and Use Tax Law. RTC section 6070.5, subdivision (b), provides that the Board may also refuse to issue a seller's permit if the person desiring to engage in or conduct business as a seller in California is not a natural person or individual and any person controlling the person desiring to engage in or conduct business as a seller within this state has an outstanding final liability as provided in subdivision (a). For purposes of subdivision (b), the word "controlling" has the same meaning as the word "controlling" as defined in Business and Professions Code section 22971. Business and Professions Code section 22971, cited in the statute, provides in relevant part:

(d)(1) "control" or "controlling" means possession, direct or indirect, of the power:
(A) To vote 25 percent or more of any class of the voting securities issued by a person.
(B) To direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, other than a commercial contract for goods or nonmanagement services, or as otherwise provided; however, no individual shall be deemed to control a person solely on account of being a director, officer, or employee of that person.
(2) For purposes of subparagraph (B) of paragraph (1), a person who, directly or indirectly, owns, controls, holds, with the power to vote, or holds proxies representing 10 percent or more of the then outstanding voting securities issued by another person, is presumed to control that other person.
(3) For purposes of this division, the board may determine whether a person in fact controls another person.

RTC section 6005 defines the term "person" for purposes of the Sales and Use Tax Law. It currently provides that the term includes "any individual, firm, partnership, joint venture, limited liability company, association, social club, fraternal organization, corporation, estate, trust, business trust, receiver, assignee for the benefit of creditors, trustee, trustee in bankruptcy, syndicate, the United States, this state, any county, city and county, municipality, district, or other political subdivision of the state, or any other group or combination acting as a unit." The word "individual," as used in RTC section 6005, refers to a natural person. A person is "not a natural person or individual" (non-natural person) referred to in RTC section 6070.5, subdivision (b), if the person is not an "individual" under RTC section 6005.

In addition, under RTC section 6070.5, subdivision (c), a liability will not be deemed to be outstanding if the person applying for a seller's permit has entered into an installment payment agreement pursuant to RTC section 6832 for the payment of the liability and is in full compliance with the terms of the installment payment agreement. However, RTC section 6070.5, subdivision (d), also provides that if the person submitting an application for a seller's permit has entered into an installment payment agreement as provided in subdivision (c) and fails to comply with the terms of the installment payment agreement, then the Board may seek revocation of the person's seller's permit obtained pursuant to the provisions of subdivision (c).

RTC section 6070.5, subdivision (e), requires the Board to provide a person with written notice of the denial of a seller's permit under RTC section 6070.5. This subdivision also provides that a person who is denied a seller's permit may seek reconsideration of the Board's denial by submitting a written request for reconsideration to the Board within 30 days of the date of the notice of denial. In addition, this subdivision provides that the Board shall provide a person submitting a timely written request for reconsideration a hearing in a manner that is consistent with a hearing provided for by RTC section 6070. However, if no written request for reconsideration is submitted within the 30-day period, the denial of the person's seller's permit becomes final at the end of the 30-day period.

Finally, RTC section 6070.5, subdivision (f), provides that the Board shall consider offers in compromise when determining whether to issue a seller's permit.

Regulation 1699 currently implements, interprets, and makes specific the provisions of RTC sections 6066, 6067, 6070, 6071.1, 6072, 6073, 6075, and 6225. As relevant here:

- Regulation 1699, subdivision (a), generally provides that every person engaged in the business of selling or leasing tangible personal property of a kind the gross receipts from the retail sale of which are subject to sales tax is required to hold a seller's permit for each place of business in this state at which transactions relating to sales are customarily negotiated with his or her customers;
- Regulation 1699, subdivision (f), currently states that a seller's permit may only be held by a person actively engaged in business as a seller of tangible personal property; and
- Regulation 1699, subdivision (f), further states that the Board may revoke a seller's permit where it finds that the person holding the permit is not actively engaged in business as a seller of tangible personal property.

Effect, Objectives, and Benefits of the Proposed Amendments to Regulation 1699

Need for Clarification

Prior to January 1, 2012, the effective date of RTC section 6070.5, if a person had an outstanding final liability with the Board and voluntarily closed its seller's permit before it was revoked under RTC section 6070, the Board could not refuse to issue another seller's permit to that person under RTC section 6070. Therefore, a person who failed to properly remit taxes and had an outstanding final liability could close out its seller's permit and then apply for a new seller's permit from the Board. And, in that situation, because the original permit was not revoked, the Board lacked the authority to refuse to issue the new permit. Under RTC section 6070.5, subdivision (a), however, the Board now has authority to refuse to issue a permit to such a person with an outstanding final liability.

In addition, prior to January 1, 2012, if a person had its seller's permit revoked under RTC section 6070 because the person failed to properly remit taxes and had an outstanding final liability, the person could still obtain a new seller's permit by transferring its business to a non-natural person that the person directly or indirectly controlled and having the non-natural person apply for the new seller's permit. For example, if the Board revoked the seller's permit held by an individual operating a business as a sole proprietorship, then the individual could:

- Form a wholly-owned corporation that the individual could directly control by owning all of the corporation's voting stock, the individual could transfer the business to the corporation, and the corporation could apply for a new seller's permit to operate the business; or

- Form a corporation that the individual's relative, such as the individual's spouse, owns and which the individual can indirectly control through means other than direct stock ownership, the individual could transfer the business to the corporation in a sale that was not at arm's length, and the corporation could apply for a new seller's permit to operate the business.

And, in either situation, the Board could not refuse to issue a seller's permit to the non-natural person, under RTC section 6070, because the non-natural person applying for the permit was not the same person who had its seller's permit revoked under RTC section 6070. Under RTC section 6070.5, subdivision (b), however, the Board now has authority to refuse to issue a seller's permit to a non-natural person applying for a new permit if the non-natural person is controlled by a person that has an outstanding final liability with the Board.

Because the enactment of RTC section 6070.5 gave the Board new authority to refuse to issue a seller's permit to a person with an outstanding final liability and to a non-natural person that is controlled by a person with an outstanding final liability, regardless of whether the person had a prior seller's permit revoked. And, there is an issue because Regulation 1699, which applies to applications for seller's permits, does not currently provide applicants with any notice regarding the Board's new authority under RTC section 6070.5 or provide clear guidance to applicants as to how the Board will implement and interpret RTC section 6070.5. Board staff determined that it was necessary to clarify Regulation 1699 to address this issue.

Interested Parties Process

As a result, Business Taxes Committee staff drafted amendments to Regulation 1699. The draft amendments suggested adding a new subdivision (g) to the regulation, renumbering the regulation's current subdivisions (g) through (j), as subdivisions (h) through (k), respectively, and adding a reference to RTC section 6070.5 to the regulation's reference note.

The draft subdivision (g) prescribed the circumstances under which the Board may refuse to issue a seller's permit to or revoke a permit from a person with an outstanding final liability or a person controlled by a person with an outstanding final liability under RTC section 6070.5. The draft subdivision (g) incorporated the definition of the words "control" and "controlling" provided in Business and Professions Code section 22971, subdivision (d)(1)(B), quoted above. The draft subdivision (g) implemented, interpreted, and made specific the definition of "control" and "controlling" for purposes of RTC section 6070.5 by establishing:

- A presumption that a person has the power to control a non-natural person if the person holds 25 percent or more of any class of the voting securities issued by the non-natural person, as provided in Business and Professions Code section 22971, subdivision (d)(1)(A);
- A presumption that a general partner has the power to control its partnership, a managing member of a limited liability company has the power to control its limited liability

company, and a president or director of a closely held corporation has the power to control its corporation; and

- A presumption that a person has the power to control a non-natural person if the person transferred its business to the non-natural person in a sale that was not at arm's length in order to address the situation (described above) in which a person with an outstanding final liability transfers its business to a non-natural person in a sale that was not at arm's length and the non-natural person applies for a new seller's permit to operate the business.

In addition, the presumption regarding whether a person has the power to control another person in draft subdivision (g) specifies that the Board will presume that a sale of a business is not at arm's length if it is between and among relatives by blood or marriage.

Business Taxes Committee staff subsequently provided its draft amendments to Regulation 1699 to the interested parties and conducted an interested parties meeting to discuss the draft amendments in July 2013. At the meeting, there were questions regarding the term "outstanding final liability."

The questions generally pertained to the nature of and the responsibility for an outstanding final liability. The interested parties wanted to know if the provisions of RTC section 6070.5 applied to certain types of outstanding final liabilities, but not others. For example, a participant asked if a person's outstanding final liability was the result of an audit performed when the person closed its business, the Board's disallowance of the person's claimed exemptions, or an "honest mistake," would those types of liabilities be sufficient for the Board to refuse to issue a seller's permit to that person? In response, staff stated that RTC section 6070.5 does not differentiate between outstanding final liabilities that result from different types of non-compliance issues, but rather, a person having any type of outstanding final liability for any amount due under the Sales and Use Tax Law may be refused a seller's permit under that section. In addition, staff explained that if a person receives a Notice of Determination for understated sales or use tax, the amount due which is not paid after the person's appeals have been exhausted and the person's liability is final is considered a final outstanding liability for purposes of RTC section 6070.5. Staff also explained that a final outstanding liability exists when a person has self-reported a tax liability, but has not paid the liability by the applicable due date.

Further, if an existing non-natural person has a final outstanding liability, an interested party wanted to know who would the liability "follow" and prevent from obtaining a seller's permit. Specifically, the participant wanted to know whether an officer who controlled a corporation with an outstanding final liability could be denied a seller's permit for a different entity due to the corporation's outstanding final liability. Staff responded that if a corporation has an outstanding final liability, the officers in control of that corporation do not automatically have an outstanding final liability for purposes of RTC section 6070.5 and cannot be denied a seller's permit for another entity based solely on the corporation's outstanding final liability. However, if the Board determines that an officer is liable for a corporation's outstanding final liability, as a "responsible person" under RTC section 6829, and any portion of the responsible person liability

remains unpaid when that determination becomes final, then the officer will have an outstanding final liability for purposes of RTC section 6070.5 that resulted from the corporation's outstanding final liability. And, in such a situation where a corporate officer is a person with an outstanding final liability, the Board may deny an application for a seller's permit for a non-natural person that is controlled by the officer under RTC section 6070.5.

Staff also noted at the July 2013 meeting that the statute is permissive and that staff's draft amendments to Regulation 1699 do not change the permissive nature of the Board's authority under the statute. Section 6070.5 gives the Board the authority not to issue seller's permits under specified circumstances. However, the statute does not require the Board to refuse to issue a seller's permit to any person with an outstanding final liability.

After the first interested parties meeting, Business Taxes Committee staff revised the draft amendments to Regulation 1699, provided the revised draft to the interested parties, and conducted a second interested parties meeting on September 3, 2013, to discuss the revised draft. The revised draft amendments included language to clarify the presumption regarding non-arm's length transactions among relatives in new subdivision (g)(3)(C). Specifically, language was added to explain that, "[a] transfer is among relatives if the person with the outstanding final liability is either a natural person who is a relative of the person or persons controlling the non-natural person acquiring the business[,] or is a non-natural person controlled by a relative or relatives of the person or persons controlling the nonnatural person acquiring the business." Staff also added language to explain that the presumptions regarding control provided in subdivision (g)(3) are rebuttable presumptions.

At the second interested parties meeting, a participant wanted to know whether the Board could issue a temporary seller's permit to a person while the person is filing a request for reconsideration of the denial of its seller's permit, and waiting for a hearing and the Board's decision on its request for reconsideration, which the participant believes could take an extensive amount of time. The argument was that the California economy could be unnecessarily harmed if the Board's initial decision to refuse to issue a business a seller's permit is based on inaccurate information or is just a bad decision, and the business is prevented from operating while it waits for a hearing and a favorable decision on its request for reconsideration. Staff's response to the question was that RTC section 6070.5 does not expressly provide for the issuance of temporary seller's permits. And, the statute does not expressly allow for the revocation of a seller's permit, except for when a person does not fulfill the terms of the installment payment agreement that they entered into in order to obtain a seller's permit. Therefore, the statute does not provide for the issuance of a temporary seller's permit to a person who was denied a seller's permit under RTC section 6070.5, and submitting a timely written request for reconsideration to the appropriate district office is a person's only option to appeal the Board's denial of a permit under that section. However, staff also explained that a person with an outstanding final liability may enter into an installment payment agreement to ensure that the person may obtain a new seller's permit. And, staff stated that through policy, the district offices will be asked to expedite their review of requests for reconsideration of denials of seller's permits under RTC section 6070.5 to reduce the time applicants have to wait to address their seller's permit issues.

At the second interested parties meeting on September 3, 2013, staff also explained that the revisions made to the draft of Regulation 1699, subdivision (g)(3), are intended to explain that a person may control a non-natural person through the "ownership of voting securities" or a "contract," but that these are just examples of how a person may control another. And, after the second interested parties meeting, staff revised subdivision (g)(3) further to clarify that the "ownership of voting securities" or the existence of a "contract" are evidence that a person may control a non-natural person and disseminated the revised language on September 5, 2013, to those interested parties who participated in the September 3, 2013, meeting. Staff did not receive any comments on its revised drafts of the amendments to Regulation 1699 by the deadline of September 19, 2013. Therefore, staff prepared Formal Issue Paper 13-008 and distributed it to the Board Members on November 8, 2013, for consideration at the Board's November 19, 2013, Business Taxes Committee meeting.

November 19, 2013 Business Taxes Committee Meeting

Formal Issue Paper 13-008 recommended that the Board approve and authorize the publication of amendments adding new subdivision (g) to Regulation 1699. As explained above, new subdivision (g) implements, interprets, and makes specific the provisions of RTC section 6070.5. It provides that the Board may refuse to issue a seller's permit to a person if they have an outstanding final liability. In addition, it provides that the Board may refuse to issue a seller's permit to a non-natural person if a person with an outstanding final liability controls the non-natural person. Further, it provides that if the Board refuses to issue a seller's permit to a person under RTC section 6070.5, the person may file a timely written request for reconsideration. Or, the person may request to enter into an installment payment agreement or an offer in compromise. Furthermore, it provides that if the installment payment agreement (or plan) is approved, a seller's permit could be issued. And, it provides that if the offer in compromise is approved and the person has paid the amount in full or remains in full compliance with the compromise plan, a seller's permit could also be issued. However, it also provides that the Board will have the authority to revoke a seller's permit if a person fails to meet the terms of the installment payment agreement or offer in compromise the person entered into to obtain the seller's permit.

During the November 19, 2013, Business Taxes Committee meeting, Chairman Horton suggested adding language to the proposed amendments to Regulation 1699 that would prohibit the Board from refusing to issue a permit to a person entering a different line of business, even if that person had an outstanding final liability from a prior business, as long as there was no financial risk to the state. The Board discussed the additional language and determined that it was not necessary at this time because the language staff recommended adding to new subdivision (g) of Regulation 1699 allows the Board to refuse to issue a seller's permit under certain circumstances, but does not require the Board to refuse to issue a seller's permit when doing so would not pose a financial risk to the state. Also, the language staff recommended adding to new subdivision (g) of Regulation 1699 provides for persons with outstanding final liabilities to enter into installment payment agreements and offers in compromise in order to

establish that they are satisfying their outstanding final liabilities and that they qualify for the issuance of a seller's permit. Therefore, new subdivision (g) already provides procedures for a person with an outstanding final liability to establish that there is no financial risk in issuing the person a seller's permit and new subdivision (g) does not prohibit the Board from issuing a seller's permit to a person when there is no longer a financial risk to the state.

No members of the public appeared at the November 19, 2013, Business Taxes Committee meeting.

Therefore, at the conclusion of the Board's discussion of Formal Issue Paper 13-008 during the November 19, 2013, Business Taxes Committee meeting, the Board Members unanimously voted to propose the amendments to Regulation 1699 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1699 are reasonably necessary to have the effect and accomplish the objectives of implementing, interpreting, and making specific RTC section 6070.5 and addressing the issue that Regulation 1699 does not currently provide applicants for seller's permits with notice of and clear guidance regarding the Board's new authority under RTC section 6070.5.

The Board anticipates that the proposed amendments will benefit applicants for seller's permits and Board staff by:

- Making Regulation 1699 consistent with RTC section 6070.5;
- Providing additional notice that an application for a seller's permit may be denied, under RTC section 6070.5, if the applicant has an outstanding final liability or the applicant is controlled by a person with an outstanding final liability;
- Helping applicants with outstanding final liabilities and applicants controlled by a person with an outstanding final liability clearly understand that their applications for seller's permits will not be denied, under RTC section 6070.5, if they take appropriate steps to pay the final liabilities, including by entering into an installment payment agreement or offer in compromise, so that the liabilities are no longer "outstanding"; and
- Alleviating potential confusion regarding the manner in which RTC section 6070.5 will be implemented and interpreted by the Board.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1699 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because there is no other state regulation implementing, interpreting, or making specific the provisions of RTC section 6070.5. In addition, the Board has determined that there are no comparable federal regulations or statutes to Regulation 1699 or the proposed amendments to Regulation 1699.

NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1699 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

NO COST OR SAVINGS TO STATE AGENCIES, LOCAL AGENCIES, AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1699 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The Board has made an initial determination that the adoption of the proposed amendments to Regulation 1699 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulation 1699 may affect small business.

NO COST IMPACTS TO 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.

RESULTS OF THE ECONOMIC IMPACT ASSESSMENT REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The Board has determined that the proposed amendments to Regulation 1699 are not a major regulation, as defined in Government Code section 11342.548 and California Code of Regulations, title 1, section 2000. Therefore, the Board has prepared the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1699 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. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulation 1699 will not affect the benefits of Regulation 1699 to the health and welfare of California residents, worker safety, or the state's environment.

NO SIGNIFICANT EFFECT ON HOUSING COSTS

The adoption of the proposed amendments to Regulation 1699 will not have a significant effect on housing costs.

DETERMINATION REGARDING ALTERNATIVES

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 the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

CONTACT PERSONS

Questions regarding the substance of the proposed amendments should be directed to Erin Dendorfer, Tax Counsel, by telephone at (916) 322-3283, by e-mail at Erin.Dendorfer@boe.ca.gov, or by mail at State Board of Equalization, Attn: Erin Dendorfer, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

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, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at Richard.Bennion@boe.ca.gov, or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

WRITTEN COMMENT PERIOD

The written comment period ends at 10:00 a.m. on March 25, 2014, or as soon thereafter as the Board begins the public hearing regarding the adoption of the proposed amendments to Regulation 1699 during the March 25, 2014, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1699. The Board will only consider written comments received by that time.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared an underscored and strikeout version of the text of Regulation 1699 illustrating the express terms of the proposed amendments. The Board has also prepared an initial statement of reasons for the adoption of the proposed amendments to Regulation 1699, which includes the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are 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 amendments and the initial statement of reasons are also available on the Board's Website at *www.boe.ca.gov.*

SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The Board may adopt the proposed amendments to Regulation 1699 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed regulation, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting regulation will be mailed to those interested parties who commented on the original proposed regulation orally or in writing or who asked to be informed of such changes. The text of the resulting regulation will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting regulation that are received prior to adoption.

AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulation 1699, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at www.boe.ca.gov.

STATE BOARD OF EQUALIZATION

BOARD APPROVED

At the [illegible] Board Meeting

Joann Richmond, Chief
Board Proceedings Division

Sincerely,

Joann Richmond

Joann Richmond, Chief
Board Proceedings Division

JR:reb

Initial Statement of Reasons for

Proposed Amendments to California Code of Regulations,

Title 18, Section 1699, *Permits*

SPECIFIC PURPOSES, PROBLEM INTENDED TO BE ADDRESSED, NECESSITY, AND ANTICIPATED BENEFITS

Current Law

In general, the Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.) requires every person desiring to engage in or conduct business as a seller of tangible personal property in California to apply to the State Board of Equalization (Board) for a seller's permit. (Rev. & Tax. Code, §§ 6014, 6066.) Under Revenue and Taxation Code (RTC) section 6070, if a person fails to comply with any provision of the Sales and Use Tax Law, such as failure to remit payment of taxes, the Board can take action to revoke the person's seller's permit. This section also states that, after a person's seller's permit is revoked, the Board shall not issue a new permit to that person until it is satisfied the person will comply with the law.

RTC section 6070.5, as enacted by Assembly Bill No. (AB) 1307 (Stats. 2011, ch. 734), authorizes the Board to refuse to issue or revoke a seller's permit under certain conditions. Prior to the enactment of RTC section 6070.5, the Board did not have express statutory authority to refuse to issue a seller's permit to a person desiring to engage in the business of selling tangible personal property in California, unless the Board had previously revoked the person's seller's permit under RTC section 6070. And, the Board sponsored the enactment of RTC section 6070.5 to "provide additional tools that would assist the [Board] in reducing its growing outstanding accounts receivable balances from [the] failure to remit the taxes that are owed . . . ." (September 9, 2011, Assembly Floor Analysis of AB 1307.)

Currently, RTC section 6070.5, subdivision (a), provides that the Board may refuse to issue a permit to any person submitting an application for a seller's permit as required under RTC section 6066 if the person desiring to engage in or conduct business as a seller in California has an outstanding final liability for any amount due under the Sales and Use Tax Law. RTC section 6070.5, subdivision (b), provides that the Board may also refuse to issue a seller's permit if the person desiring to engage in or conduct business as a seller in California is not a natural person or individual and any person controlling the person desiring to engage in or conduct business as a seller within this state has an outstanding final liability as provided in subdivision (a). For purposes of subdivision (b), the word "controlling" has the same meaning as the word "controlling" as defined in Business and Professions Code section 22971. Business and Professions Code section 22971, cited in the statute, provides in relevant part:

> (d)(1) "control" or "controlling" means possession, direct or indirect, of the power:
> (A) To vote 25 percent or more of any class of the voting securities issued by a person.

(B) To direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, other than a commercial contract for goods or nonmanagement services, or as otherwise provided; however, no individual shall be deemed to control a person solely on account of being a director, officer, or employee of that person.
(2) For purposes of subparagraph (B) of paragraph (1), a person who, directly or indirectly, owns, controls, holds, with the power to vote, or holds proxies representing 10 percent or more of the then outstanding voting securities issued by another person, is presumed to control that other person.
(3) For purposes of this division, the board may determine whether a person in fact controls another person.

RTC section 6005 defines the term "person" for purposes of the Sales and Use Tax Law. It currently provides that the term includes "any individual, firm, partnership, joint venture, limited liability company, association, social club, fraternal organization, corporation, estate, trust, business trust, receiver, assignee for the benefit of creditors, trustee, trustee in bankruptcy, syndicate, the United States, this state, any county, city and county, municipality, district, or other political subdivision of the state, or any other group or combination acting as a unit." The word "individual," as used in RTC section 6005, refers to a natural person. A person is "not a natural person or individual" (non-natural person) referred to in RTC section 6070.5, subdivision (b), if the person is not an "individual" under RTC section 6005.

In addition, under RTC section 6070.5, subdivision (c), a liability will not be deemed to be outstanding if the person applying for a seller's permit has entered into an installment payment agreement pursuant to RTC section 6832 for the payment of the liability and is in full compliance with the terms of the installment payment agreement. However, RTC section 6070.5, subdivision (d), also provides that if the person submitting an application for a seller's permit has entered into an installment payment agreement as provided in subdivision (c) and fails to comply with the terms of the installment payment agreement, then the Board may seek revocation of the person's seller's permit obtained pursuant to the provisions of subdivision (c).

RTC section 6070.5, subdivision (e), requires the Board to provide a person with written notice of the denial of a seller's permit under RTC section 6070.5. This subdivision also provides that a person who is denied a seller's permit may seek reconsideration of the Board's denial by submitting a written request for reconsideration to the Board within 30 days of the date of the notice of denial. In addition, this subdivision provides that the Board shall provide a person submitting a timely written request for reconsideration a hearing in a manner that is consistent with a hearing provided for by RTC section 6070. However, if no written request for reconsideration is submitted within the 30-day period, the denial of the person's seller's permit becomes final at the end of the 30-day period.

Finally, RTC section 6070.5, subdivision (f), provides that the Board shall consider offers in compromise when determining whether to issue a seller's permit.

California Code of Regulations, title 18, section (Regulation) 1699, *Permits*, currently implements, interprets, and makes specific the provisions of RTC sections 6066, 6067, 6070, 6071.1, 6072, 6073, 6075, and 6225. As relevant here:

- Regulation 1699, subdivision (a), generally provides that every person engaged in the business of selling or leasing tangible personal property of a kind the gross receipts from the retail sale of which are subject to sales tax is required to hold a seller's permit for each place of business in this state at which transactions relating to sales are customarily negotiated with his or her customers;
- Regulation 1699, subdivision (f), currently states that a seller's permit may only be held by a person actively engaged in business as a seller of tangible personal property; and
- Regulation 1699, subdivision (f), further states that the Board may revoke a seller's permit where it finds that the person holding the permit is not actively engaged in business as a seller of tangible personal property.

Proposed Amendments

Need for Clarification

Prior to January 1, 2012, the effective date of RTC section 6070.5, if a person had an outstanding final liability with the Board and voluntarily closed its seller's permit before it was revoked under RTC section 6070, the Board could not refuse to issue another seller's permit to that person under RTC section 6070. Therefore, a person who failed to properly remit taxes and had an outstanding final liability could close out its seller's permit and then apply for a new seller's permit from the Board. And, in that situation, because the original permit was not revoked, the Board lacked the authority to refuse to issue the new permit. Under RTC section 6070.5, subdivision (a), however, the Board now has authority to refuse to issue a permit to such a person with an outstanding final liability.

In addition, prior to January 1, 2012, if a person had its seller's permit revoked under RTC section 6070 because the person failed to properly remit taxes and had an outstanding final liability, the person could still obtain a new seller's permit by transferring its business to a non-natural person that the person directly or indirectly controlled and having the non-natural person apply for the new seller's permit. For example, if the Board revoked the seller's permit held by an individual operating a business as a sole proprietorship, then the individual could:

- Form a wholly-owned corporation that the individual could directly control by owning all of the corporation's voting stock, the individual could transfer the business to the corporation, and the corporation could apply for a new seller's permit to operate the business; or
- Form a corporation that the individual's relative, such as the individual's spouse, owns and which the individual can indirectly control through means other than direct stock ownership, the individual could transfer the business to the corporation in a sale that was not at arm's length, and the corporation could apply for a new seller's permit to operate the business.

And, in either situation, the Board could not refuse to issue a seller's permit to the non-natural person, under RTC section 6070, because the non-natural person applying for the permit was not the same person who had its seller's permit revoked under RTC section 6070. Under RTC section 6070.5, subdivision (b), however, the Board now has authority to refuse to issue a seller's permit to a non-natural person applying for a new permit if the non-natural person is controlled by a person that has an outstanding final liability with the Board.

Because the enactment of RTC section 6070.5 gave the Board new authority to refuse to issue a seller's permit to a person with an outstanding final liability and to a non-natural person that is controlled by a person with an outstanding final liability, regardless of whether the person had a prior seller's permit revoked. And, there is an issue (or problem within the meaning of Gov. Code, § 11346.2, subdivision (b)(1)) because Regulation 1699, which applies to applications for seller's permits, does not currently provide applicants with any notice regarding the Board's new authority under RTC section 6070.5 or provide clear guidance to applicants as to how the Board will implement and interpret RTC section 6070.5. Board staff determined that it was necessary to clarify Regulation 1699 to address this issue.

Interested Parties Process

As a result, Business Taxes Committee staff drafted amendments to Regulation 1699. The draft amendments suggested adding a new subdivision (g) to the regulation, renumbering the regulation's current subdivisions (g) through (j), as subdivisions (h) through (k), respectively, and adding a reference to RTC section 6070.5 to the regulation's reference note.

The draft subdivision (g) prescribed the circumstances under which the Board may refuse to issue a seller's permit to or revoke a permit from a person with an outstanding final liability or a person controlled by a person with an outstanding final liability under RTC section 6070.5. The draft subdivision (g) incorporated the definition of the words "control" and "controlling" provided in Business and Professions Code section 22971, subdivision (d)(1)(B), quoted above. The draft subdivision (g) implemented, interpreted, and made specific the definition of "control" and "controlling" for purposes of RTC section 6070.5 by establishing:

- A presumption that a person has the power to control a non-natural person if the person holds 25 percent or more of any class of the voting securities issued by the non-natural person, as provided in Business and Professions Code section 22971, subdivision (d)(1)(A);
- A presumption that a general partner has the power to control its partnership, a managing member of a limited liability company has the power to control its limited liability company, and a president or director of a closely held corporation has the power to control its corporation; and
- A presumption that a person has the power to control a non-natural person if the person transferred its business to the non-natural person in a sale that was not at arm's length in order to address the situation (described above) in which a person with an outstanding final liability transfers its business to a non-natural person in a sale that was not at arm's length and the non-natural person applies for a new seller's permit to operate the business.

In addition, the presumption regarding whether a person has the power to control another person in draft subdivision (g) specifies that the Board will presume that a sale of a business is not at arm's length if it is between and among relatives by blood or marriage.

Business Taxes Committee staff subsequently provided its draft amendments to Regulation 1699 to the interested parties and conducted an interested parties meeting to discuss the draft amendments in July 2013. At the meeting, there were questions regarding the term "outstanding final liability."

The questions generally pertained to the nature of and the responsibility for an outstanding final liability. The interested parties wanted to know if the provisions of RTC section 6070.5 applied to certain types of outstanding final liabilities, but not others. For example, a participant asked if a person's outstanding final liability was the result of an audit performed when the person closed its business, the Board's disallowance of the person's claimed exemptions, or an "honest mistake," would those types of liabilities be sufficient for the Board to refuse to issue a seller's permit to that person? In response, staff stated that RTC section 6070.5 does not differentiate between outstanding final liabilities that result from different types of non-compliance issues, but rather, a person having any type of outstanding final liability for any amount due under the Sales and Use Tax Law may be refused a seller's permit under that section. In addition, staff explained that if a person receives a Notice of Determination for understated sales or use tax, the amount due that is not paid after the person's appeals have been exhausted and the person's liability is final is considered a final outstanding liability for purposes of RTC section 6070.5. Staff also explained that a final outstanding liability exists when a person has self-reported a tax liability, but has not paid the liability by the applicable due date.

Further, if an existing non-natural person has a final outstanding liability, an interested party wanted to know who would the liability "follow" and prevent from obtaining a seller's permit. Specifically, the participant wanted to know whether an officer who controlled a corporation with an outstanding final liability could be denied a seller's permit for a different entity due to the corporation's outstanding final liability. Staff responded that if a corporation has an outstanding final liability, the officers in control of that corporation do not automatically have an outstanding final liability for purposes of RTC section 6070.5 and cannot be denied a seller's permit for another entity based solely on the corporation's outstanding final liability. However, if the Board determines that an officer is liable for a corporation's outstanding final liability, as a "responsible person" under RTC section 6829, and any portion of the responsible person liability remains unpaid when that determination becomes final, then the officer will have an outstanding final liability for purposes of RTC section 6070.5 that resulted from the corporation's outstanding final liability. And, in such a situation where a corporate officer is a person with an outstanding final liability, the Board may deny an application for a seller's permit for a non-natural person that is controlled by the officer under RTC section 6070.5.

Staff also noted at the July 2013 meeting that the statute is permissive and that staff's draft amendments to Regulation 1699 do not change the permissive nature of the Board's authority under the statute. Section 6070.5 gives the Board the authority not to issue seller's permits under

specified circumstances. However, the statute does not require the Board to refuse to issue a seller's permit to a person just because those circumstances exist.

After the first interested parties meeting, Business Taxes Committee staff revised the draft amendments to Regulation 1699, provided the revised draft to the interested parties, and conducted a second interested parties meeting on September 3, 2013, to discuss the revised draft. The revised draft amendments included language to clarify the presumption regarding non-arm's length transactions among relatives in new subdivision (g)(3)(C). Specifically, language was added to explain that, "[a] transfer is among relatives if the person with the outstanding final liability is either a natural person who is a relative of the person or persons controlling the non-natural person acquiring the business; or is a non-natural person controlled by a relative or relatives of the person or persons controlling the nonnatural person acquiring the business." Staff also added language to explain that the presumptions regarding control provided in subdivision (g)(3) are rebuttable presumptions.

At the second interested parties meeting, a participant wanted to know whether the Board could issue a temporary seller's permit to a person while the person is filing a request for reconsideration of the denial of its seller's permit and waiting for a hearing and the Board's decision on its request for reconsideration, which the participant believes could take an extensive amount of time. The argument was that the California economy could be unnecessarily harmed if the Board's initial decision to refuse to issue a business a seller's permit is based on inaccurate information or is just a bad decision, and the business is prevented from operating while it waits for a hearing and a favorable decision on its request for reconsideration. Staff's response to the question was that RTC section 6070.5 does not expressly provide for the issuance of temporary seller's permits. And, the statute does not expressly allow for the revocation of a seller's permit, except for when a person does not fulfill the terms of the installment payment agreement that they entered into in order to obtain a seller's permit. Therefore, the statute does not provide for the issuance of a temporary seller's permit to a person who was denied a seller's permit under RTC section 6070.5, and submitting a timely written request for reconsideration to the appropriate district office is a person's only option to appeal the Board's denial of a permit under that section. However, staff also explained that a person with an outstanding final liability may enter into an installment payment agreement to ensure that the person may obtain a new seller's permit. And, staff stated that through policy, the district offices will be asked to expedite their review of requests for reconsideration of denials of seller's permits under RTC section 6070.5 to reduce the time applicants have to wait to address their seller's permit issues.

At the second interested parties meeting on September 3, 2013, staff also explained that the revisions made to the draft of Regulation 1699, subdivision (g)(3), are intended to explain that a person may control a non-natural person through the "ownership of voting securities" or a "contract," but that these are just examples of how a person may control another. And, after the second interested parties meeting, staff revised subdivision (g)(3) further to clarify that the "ownership of voting securities" or the existence of a "contract" are evidence that a person may control a non-natural person and disseminated the revised language on September 5, 2013, to those interested parties who participated in the September 3, 2013, meeting. Staff did not receive any comments on its revised drafts of the amendments to Regulation 1699 by the deadline of September 19, 2013. Therefore, staff prepared Formal Issue Paper 13-008 and distributed it to

the Board Members on November 8, 2013, for consideration at the Board's November 19, 2013, Business Taxes Committee meeting.

November 19, 2013 Business Taxes Committee Meeting

Formal Issue Paper 13-008 recommended that the Board approve and authorize the publication of amendments adding new subdivision (g) to Regulation 1699. As explained above, new subdivision (g) implements, interprets, and makes specific the provisions of RTC section 6070.5. It provides that the Board may refuse to issue a seller's permit to a person if they have an outstanding final liability. In addition, it provides that the Board may refuse to issue a seller's permit to a non-natural person if a person with an outstanding final liability controls the non-natural person. Further, it provides that if the Board refuses to issue a seller's permit to a person under RTC section 6070.5, the person may file a timely written request for reconsideration. Or, the person may request to enter into an installment payment agreement or an offer in compromise. Furthermore, it provides that if the installment payment agreement (or plan) is approved, a seller's permit could be issued. And, it provides that if the offer in compromise is approved and the person has paid the amount in full or remains in full compliance with the compromise plan, a seller's permit could also be issued. However, it also provides that the Board will have the authority to revoke a seller's permit if a person fails to meet the terms of the installment payment agreement or offer in compromise the person entered into to obtain the seller's permit.

During the November 19, 2013, Business Taxes Committee meeting, Chairman Horton suggested adding language to the proposed amendments to Regulation 1699 that would prohibit the Board from refusing to issue a permit to a person entering a different line of business, even if that person had an outstanding final liability from a prior business, as long as there was no financial risk to the state. The Board discussed the additional language and determined that it was not necessary at this time because the language staff recommended adding to new subdivision (g) of Regulation 1699 allows the Board to refuse to issue a seller's permit under certain circumstances, but does not require the Board to refuse to issue a seller's permit when doing so would not pose a financial risk to the state. Also, the language staff recommended adding to new subdivision (g) of Regulation 1699 provides for persons with outstanding final liabilities to enter into installment payment agreements and offers in compromise in order to establish that they are satisfying their outstanding final liabilities and that they qualify for the issuance of a seller's permit. Therefore, new subdivision (g) already provides procedures for a person with an outstanding final liability to establish that there is no financial risk in issuing the person a seller's permit and new subdivision (g) does not prohibit the Board from issuing a seller's permit to a person when there is no longer a financial risk to the state.

No members of the public appeared at the November 19, 2013, Business Taxes Committee meeting.

Therefore, at the conclusion of the Board's discussion of Formal Issue Paper 13-008 during the November 19, 2013, Business Taxes Committee meeting, the Board Members unanimously

voted to propose the amendments to Regulation 1699 recommended in the formal issue paper.[1] The Board determined that the proposed amendments to Regulation 1699 are reasonably necessary for the specific purposes of implementing, interpreting, and making specific RTC section 6070.5, as explained above, and addressing the issue (or problem) that Regulation 1699 does not currently provide applicants for seller's permits with notice of and clear guidance regarding the Board's new authority under RTC section 6070.5.

The Board anticipates that the proposed amendments will benefit applicants for seller's permits and Board staff by:

- Making Regulation 1699 consistent with RTC section 6070.5;
- Providing additional notice that an application for a seller's permit may be denied, under RTC section 6070.5, if the applicant has an outstanding final liability or the applicant is controlled by a person with an outstanding final liability;
- Helping applicants with outstanding final liabilities and applicants controlled by a person with an outstanding final liability clearly understand that their applications for seller's permits will not be denied, under RTC section 6070.5, if they take appropriate steps to pay the final liabilities, including by entering into an installment payment agreement or offer in compromise, so that the liabilities are no longer "outstanding"; and
- Alleviating potential confusion regarding the manner in which RTC section 6070.5 will be implemented and interpreted by the Board.

The adoption of the proposed amendments to Regulation 1699 is not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to Regulation 1699.

DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 13-008, the exhibits to the issue paper, and the comments made during the Board's discussion of the issue paper during its November 19, 2013, Business Taxes Committee meeting in deciding to propose the amendments to Regulation 1699 described above.

ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulation 1699 at this time or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed

[1] The Board made three minor grammatical and formatting changes to the text of the proposed amendments to Regulation 1699, subdivision (g), recommended in Exhibit 2 to Formal Issue Paper 13-008 prior to beginning the rulemaking process. In the last sentence of subdivision (g)(3)(C), the Board changed the semicolon to a coma. In subdivision (g)(4), the Board changed "paragraph (g)(4)" to "this paragraph" in the proposed text of subdivision (g)(4)(A) and then combined the proposed text of subdivision (g)(4)(A) with the proposed text of subdivision (g)(4) so that proposed subdivision (g)(4) has two sentences and there is no longer a proposed subdivision (g)(4)(A). Also, in paragraph (g)(5), the Board changed "paragraph (g)(5)" to "this paragraph" in the proposed text of subdivision (g)(5)(A) and then combined the proposed text of subdivision (g)(5)(A) with the proposed text of subdivision (g)(5) so that proposed subdivision (g)(5) has two sentences and there is no longer a proposed subdivision (g)(5)(A).

amendments to Regulation 1699 at this time because the Board determined that the proposed amendments are reasonably necessary for the reasons set forth above.

The Board also considered whether to include the additional language recommended by Mr. Horton during the November 19, 2013, Business Taxes Committee meeting (discussed above) in the proposed amendments to Regulation 1699. However, the Board did not include the additional language in the proposed amendments to Regulation 1699 because the Board determined that the additional language was not necessary at this time (as explained above).

The Board did not reject any reasonable alternative to the proposed amendments to Regulation 1699 that would lessen any adverse impact the proposed action may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed action. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2, SUBDIVISION (b)(5) AND ECONOMIC IMPACT ASSESSMENT REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

As previously explained, RTC section 6070.5, subdivision (a), currently gives the Board the authority and discretion to refuse to issue a seller's permit to any person who has an outstanding final liability involving sales and use tax and has not entered into an installment payment agreement or offer in compromise. RTC section 6070.5, subdivision (b), also authorizes and gives the Board discretion to refuse to issue a seller's permit to a non-natural person if a person with an outstanding final liability controls the non-natural person applying for the permit. In addition, under RTC section 6070.5, subdivision (c), a liability will not be deemed to be outstanding if the person applying for a seller's permit has entered into an installment payment agreement pursuant to RTC section 6832 for the payment of the liability and is in full compliance with the terms of the installment payment agreement. However, the Board also has the authority and discretion to revoke a seller's permit obtained in conjunction with a person entering into an installment payment agreement, per RTC section 6070.5, subdivision (d), if the person fails to comply with the terms of its installment payment agreement. Further, RTC section 6070.5, subdivision (f) requires the Board to consider offers in compromise when determining whether to issue seller's permits. Furthermore, RTC section 6070.5, subdivision (e), requires the Board to provide a person with written notice of the denial of a seller's permit under RTC section 6070.5. This subdivision also provides that a person who is denied a seller's permit may seek reconsideration of the Board's denial by submitting a written request for reconsideration to the Board within 30 days of the date of the notice of denial. And, this subdivision provides that the Board shall provide a person submitting a timely written request for reconsideration a hearing in a manner that is consistent with a hearing provided for by RTC section 6070. However, if no written request for reconsideration is submitted within the 30-day period, the denial of the person's seller's permit becomes final at the end of the 30-day period. Therefore, due to the

enactment of RTC section 6070.5, there is a limited class of persons that will actually need to address outstanding final liabilities prior to obtaining a seller's permit, and some of the persons in the class will be encouraged to enter into installment payment agreements or offers in compromise to do so.

As previously explained, the proposed amendments adding new subdivision (g) to Regulation 1699:

- Provide that the Board may refuse to issue a seller's permit to a person with an outstanding final liability or a non-natural person controlled by a person with an outstanding final liability under the Sales and Use Tax Law, as expressly authorized by RTC section 6070.5, subdivisions (a) and (b);
- Provide that a final liability will not be deemed to be outstanding if the person with an outstanding final liability has entered into an installment payment agreement pursuant to RTC section 6832 and the person remains in full compliance with the terms of the installment payment agreement, as expressly provided by RTC section 6070.5, subdivisions (c);
- Provide that the Board may revoke a seller's permit if a person fails to meet the terms of the installment payment agreement entered into to obtain the seller's permit, as expressly provided by RTC section 6070.5, subdivision (d);
- Require the Board to take offers in compromise into account when determining whether to issue a seller's permit, as required by RTC section 6070.5, subdivision (f);
- Clarify that a final liability will not be deemed outstanding if the Board has accepted an offer in compromise of the final liability and the person has paid the amount in full or remains in full compliance with the compromise plan, in order to ensure that the Board takes offers in compromise into account in a manner that is consistent with the way the Board is required to take installment payment agreements into account under RTC section 6070.5, subdivisions (c);
- Clarify that the Board may revoke a seller's permit if a person fails to meet the terms of the offer in compromise entered into to obtain a seller's permit, in order to ensure that the Board takes offers in compromise into account in a manner that is fully consistent with the way the Board is required to take installment payment agreements into account under RTC section 6070.5, subdivision (d);
- Require that the Board provide written notice of the denial of a seller's permit and provide the person an opportunity to request reconsideration of the denial within 30 days, as required by RTC section 6070.5, subdivision (e); and
- Provide that the filing of a timely request for reconsideration shall afford the person a hearing in a manner that is consistent with a hearing provided for by RTC section 6070, but if a request for reconsideration is not filed within the 30-day period, the denial becomes final, as provided by RTC section 6070.5, subdivision (e).

As a result, the proposed amendments to Regulation 1699 will help ensure that individuals and businesses applying for seller's permits are aware of the provisions of RTC section 6070.5. The proposed amendments will also help individuals and non-natural persons with outstanding final liabilities and non-natural persons controlled by a person with an outstanding final liability to clearly understand that the Board now has the discretion to deny their applications for seller's

permits, under RTC section 6070.5, unless they take appropriate steps to pay the final liabilities, including by entering into an installment payment agreement or offer in compromise, so that the liabilities are no longer "outstanding."

There is nothing in the proposed amendments to Regulation 1699 that would significantly change how individuals and businesses would generally behave in response to the enactment of RTC section 6070.5, in the absence of the proposed regulatory action. Therefore, the Board estimates that the proposed amendments will not have a measurable economic impact on individuals and business that is in addition to whatever economic impact the enactment of RTC section 6070.5 has and will have on individuals and businesses. And, the Board has determined that the proposed amendments to Regulation 1699 are not a major regulation, as defined in Government Code section 11342.548 and California Code of Regulations, title 1, section 2000, because the Board has estimated that the proposed amendments will not have an economic impact on California business enterprises and individuals in an amount exceeding fifty million dollars ($50,000,000) during any 12-month period.

In addition, the proposed amendments to Regulation 1699 do not mandate that individuals or businesses apply for seller's permits, installment payment agreements, or offers in compromise, or file a request for reconsideration, and they do not mandate that the Board refuse to issue a seller's permit to any person or revoke a seller's permit issued to any person. Therefore, the Board has determined that the proposed amendments do not impose any costs on any persons, including businesses.

Furthermore, there is nothing in the proposed amendments to Regulation 1699 that would impact revenue. Therefore, based on these facts and all of the information in the rulemaking file, the Board has determined that the adoption of the proposed amendments to Regulation 1699 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.

Finally, Regulation 1699 does not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Board has also determined that the adoption of the proposed amendments to Regulation 1699 will not affect the benefits of Regulation 1699 to the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulation 1699 will not have a significant adverse economic impact on business.

The proposed amendments to Regulation 1699 may affect small businesses.

Text of Proposed Amendments to

California Code of Regulations, Title 18, Section 1699

1699. Permits.

(a) Seller's Permit In General - Number of Permits Required. Every person engaged in the business of selling (or leasing under a lease defined as a sale in Revenue and Taxation Code section 6006(g)) tangible personal property of a kind the gross receipts from the retail sale of which are required to be included in the measure of the sales tax, and only a person actively so engaged, is required to hold a seller's permit for each place of business in this state at which transactions relating to sales are customarily negotiated with his or her customers. For example, a seller's permit is required for a branch sales office at which orders are customarily taken or contracts negotiated, whether or not merchandise is stocked there.

No additional permits are required for warehouses or other places at which merchandise is merely stored and which customers do not customarily visit for the purpose of making purchases and which are maintained in conjunction with a place of business for which a permit is held; but at least one permit must be held by every person maintaining stocks of merchandise in this state for sale. However, permits are required for warehouses or other places at which merchandise is stored and from which retail sales of such merchandise negotiated out-of-state are delivered or fulfilled.

If two or more activities are conducted by the same person on the same premises, even though in different buildings, only one seller's permit is required. For example, a service station operator having a restaurant in addition to the station on the same premises requires only one seller's permit for both activities.

(b) Persons Selling in Interstate Commerce or to United States Government. A seller's permit is not required to be held by persons all of whose sales are made exclusively in interstate or foreign commerce but a seller's permit is required of persons notwithstanding all their sales (or leases under a lease defined as a sale in Revenue and Taxation Code section 6006(g)) are made to the United States or instrumentalities thereof.

(c) Persons Selling Feed. Effective April 1, 1996, a seller's permit is not required to be held by persons whose sales consist entirely of sales of feed for any form of animal life of a kind the products of which ordinarily constitute food for human consumption (food animals), or for any form of animal life not of such a kind (nonfood animals) which are being held for sale in the regular course of business, provided no other retail sales of tangible personal property are made.

If a seller of hay is also the grower of the hay, this exemption shall apply only if either:

1. The hay is produced for sale only to beef cattle feedlots or dairies, or

2. The hay is sold exclusively through a farmer-owned cooperative.

(d) Concessionaires. For the purposes of this regulation, the term concessionaire is defined as an independent retailer who is authorized, through contract with, or permission of, another retail

business enterprise (the prime retailer), to operate within the perimeter of the prime retailer's own retail business premises, which to all intents and purposes appear to be wholly under the control of that prime retailer, and to make retail sales that to the general public might reasonably be believed to be the transactions of the prime retailer. Some indicators that a retailer is *not* operating as a concessionaire are that he or she:

- Appears to the public to be a business separate and autonomous from the prime retailer. Examples of businesses that may appear to be separate and autonomous, while operating within the prime retailer's premises, are those with signs posted on the premises naming each of such businesses, those with separate cash registers, and those with their own receipts or invoices printed with their business name.

- Maintains separate business records, particularly with respect to sales.

- Establishes his or her own selling prices.

- Makes business decisions independently, such as hiring employees or purchasing inventory and supplies.

- Registers as a separate business with other regulatory agencies, such as an agency issuing business licenses, the Employment Development Department, and/or the Secretary of State.

- Deposits funds into a separate account.

In cases where a retailer is not operating as a concessionaire, the prime retailer is *not* liable for any tax liabilities of the retailer operating on his or her premises. However, if a retailer is deemed to be operating as a concessionaire, the prime retailer may be held jointly and severally liable for any sales and use taxes imposed on unreported retail sales made by the concessionaire while operating as a concessionaire. Such a prime retailer will be relieved of his or her obligation for sales and use tax liabilities incurred by such a concessionaire for the period in which the concessionaire holds a seller's permit for the location of the prime retailer or in cases where the prime retailer obtains and retains a written statement that is taken in good faith in which the concessionaire affirms that he or she holds a seller's permit for that location with the Board. The following essential elements must be included in the statement in order to relieve the prime retailer of his or her liability for any unreported tax liabilities incurred by the concessionaire:

- The seller's permit number of the concessionaire

- The location for which the permit is issued (must show the concessionaire's location within the perimeter of the prime retailer's location).

- Signature of the concessionaire

- Date

While any statement, taken timely, in good faith and containing all of these essential elements will relieve a prime retailer of his or her liability for the unreported sales or use taxes of a concessionaire, a suggested format of an acceptable statement is provided as Appendix A to this regulation. While not required, it is suggested that the statement from the concessionaire contain language to clarify which party will be responsible for reporting and remitting the sales and/or use tax due on his or her retail sales.

In instances where the lessor, or grantor of permission to occupy space, is not a retailer himself or herself, he or she is not liable for any sales or use taxes owed by his or her lessee or grantee. In instances where an independent retailer leases space from another retailer, or occupies space by virtue of the granting of permission by another retailer, but does not operate his or her business within the perimeter of the lessor's or grantor's own retail business, such an independent retailer is not a concessionaire within the meaning of this regulation. In this case, the lessor or grantor is not liable for any sales or use taxes owned by the lessee or grantee.

(e) Agents. If agents make sales on behalf of a principal and do not have a fixed place of business, but travel from house to house or from town to town, it is unnecessary that a seller's permit be obtained for each agent if the principal obtains a permit for each place of business located in California. If, however, the principal does not obtain a permit for each place of business located in California, it is necessary for each agent to obtain a seller's permit.

(f) Inactive Permits. A seller's permit may only be held by a person actively engaged in business as a seller of tangible personal property. The Board may revoke a seller's permit where it finds that the person holding the permit is not actively engaged in business as a seller of tangible personal property.

(1) Any person who holds a seller's permit but is not actively engaged in business as a seller of tangible personal property shall promptly surrender the permit by notifying the Board to cancel it.

(2) Except as explained in paragraph (3) of this subdivision, a person holding a seller's permit will be held liable for any taxes, interest, and penalties incurred, through the date on which the Board is notified to cancel the permit, by any other person who, with the permit holder's actual or constructive knowledge, uses the permit in any way. For example, a permit holder may be held liable for tax, interest, and penalty actually incurred by his or her transferee where the transferee displays the permit in his or her place of business, or uses the permit number on a resale certificate, or files sales and use tax returns under the permit number. The permit holder has the burden of establishing that the Board received notice to cancel the permit.

(A) The seller's permit holder may notify the Board by delivering the actual seller's permit to the Board with the clear request that the permit be canceled. Where the reason for cancellation is that the permit holder transferred the business, the permit holder should identify the name and address of the transferee at the time the permit is surrendered to the Board. The permit holder may also notify the Board by delivering a written statement or email to the Board that the permit holder has transferred or otherwise

ceased the business, or will do so at a specified time, and requesting that the permit be canceled. The statement should identify the name and address of the transferee, if any. The permit holder may also provide this notice to the Board orally, but it will be presumed that such notice was *not* provided unless the Board's records reflect that the permit holder clearly notified the Board of the cessation or transfer of the business for which the permit was held.

(B) The Board will also be regarded as having received notice of cancellation of the seller's permit, and the permit holder will be excused from liability for the tax, interest, and penalty incurred by another person using the permit, as of the date the Board receives actual notice of transfer of the business for which the permit was issued. It will be presumed such notice was *not* received by the Board unless the Board's records reflect that the Board received a clear notice of the cessation or transfer of the business for which the permit was held. For example, the Board's receipt of an application for a seller's permit from the transferee constitutes sufficient notice if it contains adequate information to show that the application pertains to the same business for which the permit was held. Notice to another state agency of a transfer or cessation of a business does not constitute notice to the Board. Rather, the Board must itself receive actual notice of the transfer or cessation of business.

(3) Where the seller's permit holder does not establish that the Board received actual notice of the transfer of the business for which the permit was held and is thus liable for the taxes, interest, and penalties incurred by another person using that permit, that liability is limited to the quarter in which the business was transferred and the three subsequent quarters, and shall not include any penalties imposed on the other person for fraud or intent to evade the tax. However, these limitations (liability only for the quarter in which the business was transferred and the three subsequent quarters and no fraud or intent to evade penalty) do *not* apply where, after the transfer of the business, 80 percent or more of the real or ultimate ownership of that business is held by the permit holder. For these purposes, stockholders, bondholders, partners, or other persons holding an ownership interest in an entity are regarded as having the "real or ultimate ownership" of that entity.

(g) Non-issuance or Revocation of a Seller's Permit.

(1) The Board may refuse to issue a seller's permit to any person submitting an application for a seller's permit if the person has an outstanding final liability with the Board for any amount under the Sales and Use Tax Law. The Board may also refuse to issue a seller's permit if the person applying for it is not a natural person and is being controlled by a person with an outstanding final liability for any amount under the Sales and Use Tax Law.

(2) Natural Person - A "natural person" is a living human.

(3) Control and Controlling - For the purposes of this section and as defined in Section 22971 of the Business and Professions Code, the Board defines the words "control" and "controlling" to mean the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person. Evidence that a person controls or is

controlling another person may include, but is not limited to, the ownership of voting securities, by contract, other than a commercial contract for goods or nonmanagement services, or as otherwise provided below; however, no individual shall be deemed to control a person solely on account of being a director, officer, or employee of that person. It shall be a rebuttable presumption that a person has the power to control another person if any of the following apply:

(A) A person holds 25 percent or more of any class of the voting securities issued by a person; or

(B) A person is a general partner in a partnership, a managing member of a limited liability company, or president or director of a closely held corporation; or

(C) A person with an outstanding final liability as described in paragraph (g)(1) transfers the business to a non-natural person in a sale that was not at arm's length. A sale is presumed to be not at arm's length if it is between and among relatives (by blood or marriage, which relationships include, but are not limited to, spouses, parents, children and siblings). A transfer is among relatives if the person with the outstanding final liability is either a natural person who is a relative of the person or persons controlling the non-natural person acquiring the business, or is a non-natural person controlled by a relative or relatives of the person or persons controlling the non-natural person acquiring the business.

(4) A final liability will not be deemed to be outstanding for the purposes of this part if the person with the outstanding liability as described in paragraph (g)(1) has entered into a payment plan pursuant to Revenue and Taxation Code section 6832 and remains in full compliance with it. If the person submitting an application for a seller's permit has entered into a payment plan as provided in this paragraph and fails to comply with the terms of the payment plan, the Board may seek revocation of the seller's permit obtained by the person pursuant to this section.

(5) The Board shall consider offers in compromise when determining whether to issue a seller's permit. If a seller's permit is conditioned on an offer in compromise being entered into, then a final liability will not be deemed outstanding for the purposes of this part, if the offer in compromise has been accepted by the Board and the person has paid the amount in full or remains in full compliance with the compromise plan. If the person submitting an application for a seller's permit has entered into an offer in compromise as provided in this paragraph and fails to comply with the terms of the offer in compromise, the Board may seek revocation of the seller's permit obtained by the person pursuant to this section.

(6) Whenever any person is denied a permit pursuant to this section, the Board shall give the person written notice of the denial. Any person denied a permit pursuant to this section may make a request for reconsideration by the Board, if submitted in writing within 30 days of the denial. A timely submitted written request for reconsideration shall afford the person a hearing in a manner that is consistent with a hearing provided for by Revenue and Taxation

Code section 6070. If a request for reconsideration is not filed within the 30-day period, the denial becomes final.

(~~g~~h) Due Date of Returns - Closeout of Account on Yearly Reporting Basis. Where a person authorized to file tax returns on a yearly basis transfers the business to another person or discontinues it before the end of the yearly period, a closing return shall be filed with the Board on or before the last day of the month following the close of the calendar quarter in which the business was transferred or discontinued.

(~~h~~i) Buying Companies - General

(1) Definition. For the purpose of this regulation, a buying company is a legal entity that is separate from another legal entity that owns, controls, or is otherwise related to, the buying company and which has been created for the purpose of performing administrative functions, including acquiring goods and services, for the other entity. It is presumed that the buying company is formed for the operational reasons of the entity which owns or controls it or to which it is otherwise related. A buying company formed, however, for the sole purpose of purchasing tangible personal property ex-tax for resale to the entity which owns or controls it or to which it is otherwise related in order to re-direct local sales tax from the location(s) of the vendor(s) to the location of the buying company shall not be recognized as a separate legal entity from the related company on whose behalf it acts for purposes of issuing it a seller's permit. Such a buying company shall not be issued a seller's permit. Sales of tangible personal property to third parties will be regarded as having been made by the entity owning, controlling, or otherwise related to the buying company. A buying company that is not formed for the sole purpose of so re-directing local sales tax shall be recognized as a separate legal entity from the related company on whose behalf it acts for purposes of issuing it a seller's permit. Such a buying company shall be issued a seller's permit and shall be regarded as the seller of tangible personal property it sells or leases.

(2) Elements. A buying company is not formed for the sole purpose of re-directing local sales tax if it has one or more of the following elements:

(A) Adds a markup to its cost of goods sold in an amount sufficient to cover its operating and overhead expenses.

(B) Issues an invoice or otherwise accounts for the transaction.

The absence of any of these elements is not indicative of a sole purpose to redirect local sales tax.

(~~i~~j) Web Sites. The location of a computer server on which a web site resides may not be issued a seller's permit for sales tax purposes except when the retailer has a proprietary interest in the server and the activities at that location otherwise qualify for a seller's permit under this regulation.

(~~j~~k) Use Tax Permit - Qualified Purchasers. Except for the purchase of a vehicle, vessel, or aircraft, a person who meets all of the following conditions is required to register and report and pay use tax directly to the Board:

(1) The person is not required to hold a seller's permit.

(2) The person is not required to be registered pursuant to Revenue and Taxation Code section 6226.

(3) The person is not a holder of a use tax direct payment permit as described in Revenue and Taxation Code section 7051.3.

(4) The person receives at least one hundred thousand dollars ($100,000) in gross receipts from business operations per calendar year.

(5) The person is not otherwise registered with the board to report use tax.

The return must show the total sales price of the tangible personal property purchased by the qualified purchaser, the storage, use, or other consumption of which became subject to the use tax during the preceding calendar year, for which the qualified purchaser did not pay tax to a retailer required to collect the tax or a retailer the qualified purchaser reasonably believed was required to collect the tax. Notwithstanding Revenue and Taxation Code sections 6451, 6452, 6452.1, and 6455, the returns for the 2009 calendar year and subsequent years shall be filed with the Board, together with a remittance of the amount of the tax due, on or before April 15 of the succeeding calendar year.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6066, 6067, 6070, 6070.5, 6071.1, 6072, 6073, 6075 and 6225, Revenue and Taxation Code.

Regulation History

Type of Regulation: Sales and Use Tax

Regulation: 1699

Title: 1699, *Permits*

Preparation: Erin Dendorfer
Legal Contact: Erin Dendorfer

The proposed amendments to Regulation 1699, *Permits,* incorporate and clarify Revenue and Taxation Code section 6070.5's provisions authorizing the Board to refuse to issue seller's permits under specified circumstances.

History of Proposed Regulation:

March 25, 2014	Public Hearing
February 7, 2014	OAL publication date; 45-day public comment period begins; Interested Parties mailing
January 28, 2014	Notice to OAL
November 19, 2013	Business Tax Committee, Board Authorized Publication (Vote 5-0)

Sponsor:	NA
Support:	NA
Oppose:	NA