

## Memorandum

**To:** Honorable Jerome E. Horton, Chairman  
Senator George Runner, Vice Chair  
Honorable Fiona Ma, CPA, Second District  
Honorable Diane L. Harkey, Fourth District  
Honorable Betty T. Yee, State Controller

**Date:** March 12, 2015

**From:**   
Randy Ferris  
Chief Counsel

**Subject:** Board Meeting, March 25-26, 2015  
Chief Counsel Matters – Item J. Rulemaking  
Petition to Repeal Sales and Use Tax Regulation 1585,  
*Cellular Telephones, Pagers, and Other Wireless Telecommunication Devices*

On Monday, February 23, 2015, the Legal Department received a petition dated February 18, 2015 (attached hereto with related correspondence dated March 7, 2015), from Ms. Jenny Lee (petitioner), pursuant to Government Code section 11340.6, requesting the repeal of California Code of Regulations, title 18, section (Regulation or Reg.) 1585, *Cellular Telephones, Pagers, and Other Wireless Telecommunication Devices*, or, alternatively, the repeal of subdivisions (a)(3) and (4), (b)(3) through (6), and (c) of Regulation 1585. The petition seeks to repeal the regulation or the portions of the regulation clarifying the measure of tax with regard to sales of wireless telecommunications devices in “bundled” transactions because petitioner asserts that the regulation is inconsistent with the statutory definition of “gross receipts” in Revenue and Taxation Code (RTC) section 6012.

This matter is scheduled for the Board’s consideration at the March 25-26, 2015, Board meeting on the Chief Counsel Matters Agenda. At the meeting, the Board may: (1) deny the petition; (2) grant the petition in part or in whole and commence the official rulemaking process to repeal or amend the regulation by ordering publication of a notice pursuant to Government Code section 11346.5; (3) direct staff to commence an interested parties process to consider the requested repeal or amendments in part or in whole; or (4) take any other action the Board deems appropriate. Staff recommends that the Board deny the petition in its entirety because, as explained below, Regulation 1585’s provisions clarifying the measure of tax with regard to sales of wireless telecommunications devices in bundled transactions are consistent with the definition of “gross receipts” in RTC section 6012 and judicial precedent interpreting that definition. In staff’s view, the petition appears to be based on petitioner’s misinterpretation of current law.

This memorandum sets forth: (1) relevant background information pertaining to the drafting and adoption of Regulation 1585 and to staff’s response to the petition; (2) a discussion of and staff’s response to the petition; and (3) staff’s recommendation.

## I. Background Information

### A. *Sales and Use Tax*

California imposes sales tax on retailers for the privilege of selling tangible personal property at retail. (RTC, § 6051.) Unless an exemption or exclusion applies, the tax is measured by a retailer's gross receipts from the retail sale of tangible personal property in California. (RTC, § 6051.) Although sales tax is imposed on retailers, retailers may collect sales tax reimbursement from their customers if their contracts of sale so provide. (Civ. Code, § 1656.1; Reg. 1700, subd. (a)(1).) If a retailer collects sales tax reimbursement that is computed on an amount that is not taxable or on an amount in excess of the taxable amount, the retailer is required to return the excess amount paid to the customer. (RTC, § 6901.5; Reg. 1700, subd. (b).)

When sales tax does not apply, use tax is imposed, measured by the sales price of property purchased from a retailer for storage, use, or other consumption in California. (RTC, §§ 6201, 6401.) The use tax is imposed on the person actually storing, using, or otherwise consuming the property. (RTC, § 6202.) Every retailer "engaged in business" in California that makes sales subject to California use tax is required to collect the use tax from its customers and remit it to the Board, and such retailers are liable for California use tax that they fail to collect from their customers and remit to the Board. (RTC, § 6203; Reg. 1684.) However, a consumer remains liable for reporting and paying use tax to the Board when the use tax is not paid to a retailer that is registered to collect the tax. (Reg. 1685, subd. (a).) In addition, RTC section 6901 expressly provides for the Board to refund overpaid use tax to a consumer that reported and paid the use tax to the Board, and for the Board to refund directly to a consumer "[a]ny overpayment of the use tax by [the consumer] to a retailer who is required to collect the tax and who gives the purchaser a receipt therefor." (RTC, § 6901; Reg. 1685, subd. (a).)

RTC sections 6011 and 6012 similarly define the terms "sales price" and "gross receipts" so that the measure of tax is substantially the same with respect to sales and use tax transactions. In relevant part, RTC section 6012, subdivisions (a)(1) and (2), and (b)(1) through (3), expressly provide that:

- (a) "Gross receipts" mean the total amount of the sale or lease or rental price, as the case may be, of the retail sales of retailers, valued in money, whether received in money or otherwise, without any deduction on account of . . . (1) The cost of the property sold. . . [or] (2) The cost of the materials used, labor or service cost, interest paid, losses, or any other expense.
- (b) The total amount of the sale or lease or rental price includes all of the following:
  - (1) Any services that are a part of the sale.
  - (2) All receipts, cash, credits and property of any kind.
  - (3) Any amount for which credit is allowed by the seller to the purchaser.

As relevant here, the Board's long-standing interpretation of RTC section 6012 is that "'[s]ervices that are a part of the sale' include any the seller must perform in order to produce and sell the property, or for which the purchaser must pay as a condition of the purchase and/or functional use of the property, even where such services might not appear to directly relate to production or

sale costs.” (See, e.g., Sales and Use Tax Annotation<sup>1</sup> 295.1690 (8/16/78).) Also, the California court’s and the Board’s long-standing interpretations of RTC section 6012 are that a retailer’s gross receipts include all of the retailer’s receipts from the sale of tangible personal property, not solely amounts that the retailer actually received directly from a consumer. (See, e.g., *Anders v. State Board of Equalization* (1947) 82 Cal.App.2d 88 [gross receipts included non-mandatory tips paid to retailer’s waitresses for serving food to the extent waitresses agreed to credit the tips against retailer’s obligation to pay minimum wage]; Sales and Use Tax Annotation 295.0430 (5/9/73) [amount received from a manufacturer as reimbursement for accepting the manufacturer’s coupon from the customer is included in gross receipts].) In addition, retailers may collect sales tax reimbursement from their customers on the full amount of their gross receipts from the sale of tangible personal property, including amounts received from third parties, if their contracts of sale so provide. (Sales and Use Tax Annotation 295.1045 (3/11/93).)

### *B. Drafting and Adoption of Regulation 1585*

It is a common practice in the wireless telecommunication industry for a retailer to offer to sell a wireless telecommunication device for a fair retail price (cost plus a mark-up) and for the retailer to offer to sell the same device for a discounted price if the sale of the device is coupled (or bundled) with the purchase of wireless telecommunication service because the wireless service provider will indirectly reimburse the retailer for giving the consumer a discount on the device, similar to the manner in which a manufacturer may reimburse a retailer for accepting the manufacturer’s coupon. However, this practice first started to become prevalent after the California Public Utilities Commission reversed the long-standing ban against “bundling” in 1995. Board staff worked closely with retailers of wireless telecommunication devices and wireless telecommunications service providers to provide clear and administratively efficient guidance regarding the application of the Sales and Use Tax Law to sales of wireless telecommunications devices in bundled transactions when the practice was new. Thus, the provisions ultimately included in Regulation 1585, which the Board adopted on October 15, 1998, are the result of a collaborative effort between retailers of wireless telecommunication devices, wireless telecommunications service providers, and the Board.

Board staff discussed its first formal draft of Regulation 1585 in Formal Issue Paper 97-017 (dated current as of December 17, 1997), which Board staff submitted to the Board for consideration at its January 6, 1998, Business Taxes Committee (BTC) meeting. (For your reference, the formal issue paper is also attached hereto.) During the January 6, 1998, BTC meeting, the wireless telecommunications industry indicated that it still had some concerns about the specific language staff used to prescribe the application of tax to bundled and unbundled transactions in staff’s first formal draft of Regulation 1585. The wireless telecommunications industry also indicated that it had substantive objections to staff’s proposed application of tax to “carrier restricted transactions” and “retail utilities transactions” in subdivisions (a)(4) and (5), and (b)(2) and (3) of staff’s first draft of the Regulation. Therefore, the Business Taxes Committee approved publication of a second January 6, 1998, version of Regulation 1585, which included some changes that both staff and the wireless telecommunications industry agreed to, and advised industry to continue to express whatever concerns they still had regarding the specific regulatory language and provide

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<sup>1</sup> Annotations do not have the force or effect of law, but are intended to provide guidance regarding the interpretation of the Sales and Use Tax Law with respect to specific factual situations. (Reg. 5700, subs. (a)(1), (c)(2).)

specific alternative language for the Board's consideration. (January 6, 1998, Business Taxes Committee meeting minutes.)

The Board subsequently published the January 6, 1998, draft of Regulation 1585, and held a public hearing regarding the adoption of that draft on April 30, 1998. Several written comments were received from the wireless telecommunications industry before the public hearing and several comments were made by industry representatives during the public hearing. "The Board, as a result of the written and oral comments discussed above, concluded that, as the published version was an initial draft published to get the regulation process going, further work would be needed. Thereupon the Board closed the Public Hearing, without approving specific changes, and ordered staff to work with industry to develop a final version to be presented to the Board . . . ." (Final Statement of Reasons, p. 4.)

The Board's reconsideration of Regulation 1585 was subsequently postponed twice while Board staff and industry worked together during several informal meetings. Finally, on August 18, 1998, Board staff submitted a revised draft of Regulation 1585 for the Board's consideration during its August 27, 1998, meeting, which addressed the majority of industry's drafting issues and no longer recommended that Regulation 1585 include the provisions regarding "carrier restricted transactions" and "retail utilities transactions." On August 27, 1998, the Board gave staff direction regarding the remaining drafting issues. For example, "[i]n the August 18, 1998 draft, the staff had recommended that a markup of 30% . . . be used [to determine whether a device was sold at a fair retail selling price]; industry proposed a markup of 6%. . . the Board compromised, amending the staff draft to specify a markup of 18%." (Final Statement of Reasons, p. 6.) Also, the Board added a new provision stating that "the measure of tax for unbundled transactions made prior to October 1, 1995 was the actual consideration received from the end-use customer. Under Revenue and Taxation Code section 7051, the Board concluded that October 1 was a proper date on the grounds that (1) the date, not capable of being determined with exactitude, should be the start of a tax period, and (2) this was the date that the Board had issued a Notice to industry as to how tax should be applied to sales of devices in bundled transactions, and the Board concluded that such transactions had been reported under this formula ever since." (Final Statement of Reasons, p. 7.)

On August 27, 1998, the Board also approved the changes the Board directed staff to make to the August 18, 1998, draft of Regulation 1585. A new draft, dated August 31, 1998, was created. The August 31, 1998, draft of Regulation 1585 was provided to the interested parties on September 15, 1998, and the interested parties were given an additional 15 days in which to submit any remaining comments they had regarding the proposed language. However, no written or oral comments were received. Consequently, the Board Members unanimously voted to adopt the August 31, 1998, version of Regulation 1585 during the Board's meeting on October 15, 1998. (Final Statement of Reasons, p. 8.)

As relevant here, the current provisions of subdivision (a)(4) of Regulation 1585 define the unbundled sales price of a wireless telecommunication device as the actual "price at which the retailer has sold [such] specific wireless telecommunication devices to customers who are not required to activate or contract for utility service with the retailer or with an independent wireless telecommunications service provider for utility service as a condition of that sale." The current provisions of subdivision (a)(3) of Regulation 1585 clarify for retailers that a bundled transaction is an agreement for the sale of a wireless telecommunication device that "contractually requires the retailer's customer to activate or contract with a wireless telecommunications

service provider for utility service for a period greater than one month as a condition of that sale.” The current provisions of subdivision (b)(3) of Regulation 1585 also clarify for retailers that, in bundled transactions where the customers are paying the retailers a discounted sales price for a wireless telecommunication device and wireless telecommunications service providers are paying the retailers rebates or commissions for selling the devices at discounted prices with the required services, the retailers’ gross receipts from the sale of the devices are limited to the unbundled sales prices of the devices as determined from actual sales, and do not include any amounts in excess of the unbundled sales prices. In addition, the current provisions of subdivision (a)(4) of Regulation 1585 provide an objective and administratively efficient way of reporting tax for retailers who cannot establish the unbundled sales price of a wireless telecommunication device by looking at an actual unbundled sale of the device. Subdivision (a)(4) provides that these retailers shall report and pay tax on the fair retail selling price of the device, which is equal to the cost of the device plus a markup on cost of at least 18 percent.

#### *C. Regulation 1671.1, Discounts, Coupons, Rebates, and Other Incentives*

The Board has also adopted Regulation 1671.1, *Discounts, Coupons, Rebates, and Other Incentives*, to generally prescribe the measure of tax when retailers receive consideration from third parties for making discounted sales of tangible personal property to consumers. Regulation 1671.1 does not currently apply to sales of wireless telecommunication devices under Regulation 1585 because the specific provisions of Regulation 1585, not the general provisions of Regulation 1671.1, are controlling for the wireless telecommunication industry. However, it should be noted that, while not currently applicable, Regulation 1671.1, subdivision (c)(3)(A) provides that “when a retailer enters into an oral or written contract with a manufacturer or other third party that requires, on a transaction-by-transaction basis, a specific reduction in the retailer’s selling price of specified products in exchange for a certain payment of a like amount from the contracting party . . . , such payments received by the retailer are part of the taxable gross receipts or sales price of the sales.”

#### *D. The Court’s Deference to the Board’s Regulations*

The California Supreme Court has previously reviewed challenges to the Board’s interpretations of tax laws, both with and without the adoption of regulations. In *Yamaha Corporation of America v. State Board of Equalization* (1998) 19 Cal.4th 1, 10-11 (hereafter *Yamaha*), the California Supreme Court explained that:

It is a “black letter” proposition that there are two categories of administrative rules and that the distinction between them derives from their different sources and ultimately from the constitutional doctrine of the separation of powers. One kind – quasi-legislative rules – represents an authentic form of substantive lawmaking: Within its jurisdiction, the agency has been delegated the Legislature’s lawmaking power. [Citations omitted.] Because agencies granted such substantive rulemaking power are truly “making law,” their quasi-legislative rules have the dignity of statutes. When a court assesses the validity of such rules, the scope of its review is narrow. If satisfied that the rule in question lay within the lawmaking authority delegated by the Legislature, and that it is reasonably necessary to implement the purpose of the statute, judicial review is at an end.

In *Yamaha*, the Court also quoted its earlier case, *Wallace Berrie & Company v. State Board of Equalization* (1985) 40 Cal.3d 60, 65, which similarly held that:

“‘[I]n reviewing the legality of a regulation adopted pursuant to a delegation of legislative power, the judicial function is limited to determining whether the regulation (1) is “within the scope of the authority conferred” [citation] and (2) is “reasonably necessary to effectuate the purpose of the statute” [citation].’ [Citation.] ‘These issues do not present a matter for the independent judgment of an appellate tribunal; rather, both come to this court freighted with [a] strong presumption of regularity . . . .’ [Citation.] Our inquiry necessarily is confined to the question whether the classification is ‘arbitrary, capricious or [without] reasonable or rational basis.’ . . .” (*Yamaha*, at p. 11.)

In *Yamaha*, the Court also said that judicial review is more deferential when the Board has adopted a quasi-legislative regulation, pursuant to the Administrative Procedure Act, codifying its interpretation of a statute (*Yamaha*, p. 13), and that an administrative interpretation in such a regulation “will be accorded great respect by the courts and will be followed if not clearly erroneous.” (*Yamaha*, at p. 7.)

Furthermore, the California Supreme Court has previously rejected arguments that a Board regulation is invalid simply because it does not apply to different, but comparable, types of transactions. The Court affirmed that, to prevail against such an argument, the Board only needs to establish that the regulation is “not arbitrary, capricious, or without a rational basis.” (*Western States Petroleum Association v. Board of Equalization* (2013) 57 Cal.4th 401, 421.)

#### *E. Yabsley v. Cingular Wireless LLC & Loeffler v. Target Corporation*

In *Yabsley v. Cingular Wireless, LLC* (Santa Barbara County Superior Court Case No. 01221332, Second Dist. Ct. of Appeal Case No. B198827, and Supreme Court Case No. S176146) (hereafter *Yabsley*), Cingular advertised that it would sell a cellular phone by itself for \$299.99 and that it would sell the same cellular phone for 50 percent less or \$149.99 in a bundled transaction with a Cingular wireless calling plan. The plaintiff purchased the cell phone in a bundled transaction with the wireless services, and, as a result, Cingular collected sales tax reimbursement from plaintiff measured by the unbundled price of the phone, based on Regulation 1585. In addition, Cingular did so without expressly informing the plaintiff prior to the sale that the tax would be based on the unbundled price of the phone. However, the amount of tax reimbursement was shown on the sales invoice furnished to the plaintiff at the time of sale.

The plaintiff alleged that Cingular engaged in unfair competition and misleading advertising in violation of Business and Professions Code sections 17200 and 17500. Cingular argued that its application of the sales tax to its sale of the cell phone was specifically authorized under the Board’s regulation, so it could not be held liable for engaging in unfair business practices. The trial court agreed, granting Cingular’s demurrer without leave to amend. The Court of Appeal also agreed, ruling that the Board’s regulations have the force and effect of law; therefore, business activities permitted by the Board’s regulation could not be unlawful or unfair. The Court of Appeal’s opinion was published on August 18, 2008, as 165 Cal.App.4th 1526.

On September 17, 2008, however, the court vacated its opinion at the request of the California Attorney General, who had not been served with the briefs as required by applicable law. After briefing resumed, the Attorney General filed an *amicus* brief reflecting the Department of Justice's (DOJ's) *own* position that consumer protection laws could be used to adjudicate matters relating to sales taxes. The Board authorized the Legal Department to file an *amicus* brief opposing the position taken by the DOJ as contrary to the Board's regulations. Subsequently, the court issued an opinion affirming its previous ruling and also concluding that consumer protection statutes could not be used to adjudicate tax issues. The court's opinion was based in part on the reasoning in the Court of Appeal's recent decision, at the time, in *Loeffler v. Target Corporation* (2009) 173 Cal.App.4th 1229 (hereafter *Loeffler*), another case brought under consumer protection statutes challenging Target's collection of sales tax reimbursement on sales of hot coffee "to go," that such consumer protection suits regarding tax issues were barred by article XIII, section 32, of the California Constitution. The Court of Appeal's second *Yabsley* opinion was published on August 19, 2009, as 176 Cal.App.4th 1156.

Subsequently, the California Supreme Court granted review of *Yabsley*, but deferred its review pending its consideration of the related consumer protection issues in *Loeffler* (S1723972); and the Court of Appeal's second published opinion was depublished, pursuant to Rule 8.1105 of the California Rules of Court, as a procedural result of the grant of review. Then, the California Supreme Court decided *Loeffler* (2014) 58 Cal.4th 1081, 1092, holding that the RTC "provides the exclusive means by which plaintiffs' dispute over the taxability of a retail sale may be resolved and that their current lawsuit is inconsistent with tax code procedures. . . . [T]he consumer protection statutes under which plaintiffs brought their action cannot be employed to avoid the limitations and procedures set out by the Revenue and Taxation Code." Therefore, the California Supreme Court dismissed its review of *Yabsley* without expressly ordering the Court of Appeal's 2009 opinion in *Yabsley* to be re-published, so the Court of Appeals decision in *Yabsley* became final, but its 2009 opinion in *Yabsley* is still depublished today.<sup>2</sup>

#### *F. Legislative Efforts to Change the Measure of Tax Regarding Sales of Wireless Devices*

The Legislature is aware of Regulation 1585 and how it applies to bundled transactions involving sales of wireless telecommunication devices. From the 2001-2002 legislative session through the current legislative session, the following four bills were considered, but none were approved, that would have added section 6012.4 to the Revenue and Taxation Code to provide that "'gross receipts' and 'sales price' from the retail sale of a wireless [telecommunication or communication] device shall be limited to the amount charged for the sale of the wireless telecommunication device when that device is sold in a bundled transaction":

- Assembly Bill No. (AB) 2691 (2013-2014 session) – held in the Assembly Revenue and Taxation Committee;
- Senate Bill No. 1086 (2011-2012 session) – failed passage in the Senate Committee on Governance and Finance;
- AB 279 (2011-2012 session) – held in the Assembly Revenue and Taxation Committee; and
- AB 2320 (2005-2006 session) – held in the Assembly Revenue and Taxation Committee.

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<sup>2</sup> The Court of Appeal's unpublished 2009 opinion in *Yabsley* is discussed in order to provide relevant historical background information. It is not being cited as precedent.

Board staff's April 29, 2014, Legislative Bill Analysis of the most recent bill, AB 2691, included staff's estimate that the enactment of RTC section 6012.4 would result in the annual loss of approximately \$383 million in state and local sales and use tax revenue.

## II. Discussion of the Petition

The petition requests that the Board repeal Regulation 1585 or, alternatively, that the Board repeal subdivisions (a)(3) and (4) (defining bundled transaction and unbundled sales price), (b)(3) through (6) (regarding the application of tax to bundled transactions, activation fees, consignment or sales and return transactions, and sales at less than 50 percent of cost), and (c) (regarding bad-debt deductions) of Regulation 1585. The petition seeks to repeal the regulation or portions of the regulation because petitioner asserts that the regulation is inconsistent with the statutory definition of "gross receipts" in RTC section 6012 and, therefore, violates Government Code sections 11342.1, which requires that an enforceable regulation be within the scope of the adopting agency's rulemaking authority, and 11342.2, which requires that a regulation be "consistent and not in conflict with the statute" it is implementing, interpreting, or making specific and be reasonably necessary to effectuate the purpose of the statute.

The petition generally alleges that the Board "exceeded its authority in the promulgation of Regulation 1585 because the regulation is inconsistent with the California Revenue and Taxation Code's requirement that all sales taxes are to be calculated based on the 'gross receipts' retailers actually receive at the point of sale. See Rev. & Tax. Code §§ 6012 and 6051. The [r]egulation wrongly and unlawfully redefines 'gross receipts' to include an imaginary, and arbitrary, dollar amount that is not actually received by the retailer for the transaction." (Petition, p. 2.)

The petition also more specifically alleges that the Board "wrongly promulgated in Regulation 1585 that the 'gross receipts' from mobile phone sales be measured by the 'unbundled sales price' of the phone, even when the actual price charged and received by the retailer is significantly lower. Rev. & Tax. Code §[ ] 6012(a) defines 'gross receipts' as the total amount of money received by the retailer for the transaction. In Regulation 1585, the [Board] acknowledges that sales tax must be applied 'to the gross receipts from the retail sale of a wireless telecommunication device sold in a bundled transaction,' but then unilaterally and unlawfully specifies that the bundled transaction be 'measured by the unbundled sales price of the device.' See Regulation 1585(b)(3)." (Petition, pp. 3-4.) The petition further states that "[c]ontrary to the clear language in the Tax Code, Regulation 1585 unlawfully redefines 'gross receipts' – and does so only with regard to mobile phones and other wireless telecommunication devices – to include an imaginary, and arbitrary, dollar amount that is not actually received by the retailer for the transaction." (Petition, p. 5.)

In addition, the petition explains why the petitioner filed the petition. The petition states that "[o]n December 27, 2012, [petitioner] purchased an iPhone 5 for \$199.99" and "[o]n December 18, 2013, [petitioner] purchased an LG Optimo G Pro mobile phone for \$99.99" from the same AT&T's retail store in San Francisco, and that in both instances petitioner "purchased the phones as part of a bundled transaction where she was required to sign a two-year contract with AT&T as her wireless carrier." (Petition, p. 2.) Petitioner's receipt from the first transaction shows that petitioner paid "\$199.99" for the iPhone 5 because petitioner received a \$450 "commitment savings" credit on the \$649.99 sales price of the iPhone 5 before the credit, and shows that petitioner paid the retailer "\$55.25" of sales tax reimbursement on the \$649.99 unbundled sales price of the iPhone 5 before the credit. (Exhibit A to Petition.) Petitioner's receipt from the

second transaction shows that petitioner paid “\$99.99” for the LG Optimo because petitioner received a \$340 “commitment savings” credit on the \$439.99 sales price of the LG Optimo before the credit, and shows that petitioner paid the retailer “\$38.50” of sales tax reimbursement on the \$439.99 unbundled sales price of the LG Optimo before the credit. (Exhibit A to Petition.) Petitioner alleges she “overpaid sales tax on the transactions in the amount of \$68.00, which is the difference between the taxes she did pay (based on the fictitious \$649.99 and \$349.99 prices), and the taxes she would have paid if not for Regulation 1585 (based on the true \$199.99 and \$99.99 prices).” Petitioner also alleges that she “is representative of millions of California consumers who have paid, and continue to pay, excessive sales taxes pursuant to the unlawful Regulation 1585.”

Regulation 1585’s purpose is to specifically address the application of the Sales and Use Tax Law to sales and purchases of wireless telecommunication devices. As explained above, and as applicable to the petition’s alleged facts, Regulation 1585 defines the unbundled sales price of a wireless telecommunication device, such as an iPhone 5, as the actual “price at which the retailer has sold [such] specific wireless telecommunication devices to customers who are not required to activate or contract for utility service with the retailer or with an independent wireless telecommunications service provider for utility service as a condition of that sale.” (Reg. 1585, subd. (a)(4).)

As discussed above, when available, the unbundled sales price is based on the actual price of the same wireless telecommunication device when sold in an unbundled transaction where the retailer does not receive consideration from a third party. Also, the unbundled sales price is only based on the “fair retail value” (generally the cost of the device plus an 18-percent markup) of a wireless telecommunications device in those cases where there are no unbundled sales of the device to use as an objective measure of tax, and the fair retail value is itself a reasonable estimate of the total consideration paid by both the consumer and the wireless telecommunications service provider to a retailer for the sale of a wireless telecommunications device in a bundled transaction, and no more. Therefore, Board staff has determined that Regulation 1585’s provisions providing that sales and use tax applies to the unbundled sales price of wireless telecommunication devices sold in bundled transactions have a rational basis and are consistent with the definition of gross receipts in RTC section 6012, as interpreted by the courts and the Board. Accordingly, there is no evidence that the provisions are arbitrary, capricious, or clearly erroneous.

In addition, based upon the California Supreme Court’s opinion in *Yamaha*, the Board’s adoption of Regulation 1585 should be upheld because: (1) it is a quasi-legislative regulation; (2) its adoption was well within the Board’s broad authority, under RTC section 7051, to adopt regulations for the administration and enforcement of the Sales and Use Tax Law; and (3) it was reasonably necessary for the Board to adopt Regulation 1585 to implement the provisions of RTC sections 6011 and 6012 as they relate to the unique and various types of bundled transactions involving sales of wireless telecommunication devices that started to appear in 1995.

Further, Regulation 1585 provides much needed certainty to all retailers of wireless telecommunication devices, including retailers required to collect use tax, regarding the gross receipts from or the sale price of wireless telecommunication devices sold in bundled transactions. Moreover, the repeal of Regulation 1585 would likely create much confusion for

retailers and may even create additional record keeping requirements for them. For example, if the specific provisions of Regulation 1585 were to be repealed with no additional rulemaking specifically prescribing the measure of tax with regard to sales of wireless telecommunication devices in bundled transactions, then, by default, the general provisions of Regulation 1671.1 may apply to sales of wireless telecommunication devices in bundled transactions. Thus, when a retailer enters into a contract with a manufacturer or third party that requires, on a transaction-by-transaction basis, a specific reduction in the retailer's selling price of specified products for a certain payment, such payments received by the retailer are part of the taxable gross receipts or sales price of the sales. Regulation 1671.1 would require such retailers to include in the measure of tax all the consideration they receive from wireless telecommunications service providers from such sales of wireless telecommunication devices at specified discounted prices and require such retailers to maintain records of such consideration.

In the event that retailers did not enter into such contracts as contemplated by Regulation 1671.1 with manufacturers or third parties, in the absence of any regulatory guidance, it appears that the statutes would require that all consideration received for the sale of the wireless telecommunication devices in a bundled transaction, whether from the customer or some other party, would be included in the measure subject to tax. This would include any payments promised to the retailer by a third party. Accordingly, without the "safe harbor" of Regulation 1585, this could result in a substantial increase in the measure subject to tax upon the sale of a wireless telecommunication device. Such a result could also require substantial recordkeeping by a retailer.

Furthermore, as discussed above, the Legislature has specifically considered whether to change the application of tax to sales of wireless telecommunications devices in bundled transactions on four separate occasions and has declined to do so. In other words, the Legislature has repeatedly acquiesced to the Board's duly promulgated interpretation of RTC sections 6011 and 6012, as applied to sales of wireless telecommunication devices in bundled transactions, set forth in Regulation 1585.

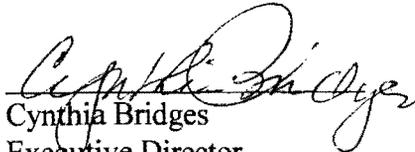
Here, the petition only generally alleges that Regulation 1585 conflicts with RTC section 6012. The petition does not quote any specific portion of RTC section 6012 with which the regulation purportedly conflicts. Rather, the petition merely makes the unsupported assertion that the Revenue and Taxation Code requires "that all sales taxes are to be calculated based on the 'gross receipts' retailers actually receive at the point of sale." As discussed above, this assertion is not an accurate interpretation of current law. (See, e.g., *Anders v. State Board of Equalization* (1947) 82 Cal.App.2d 88; Reg. 1671.1.) Additionally, the petition does not provide any new information concerning the consideration that wireless telecommunication device retailers currently receive from wireless telecommunications service providers for selling devices at discounted prices in bundled transactions. Therefore, based upon the above analysis, the petition provides no basis that would warrant any changes to Regulation 1585.

### III. Recommendation

Board staff recommends that the petition be denied in so far as it seeks the repeal of Regulation 1585 or portions thereof because the regulation is substantively valid and still necessary to prescribe the application of tax to sales of wireless telecommunication devices in bundled transactions.

If you need more information or have any questions, please contact Assistant Chief Counsel Robert Tucker at (916) 322-0437.

Approved:

  
 Cynthia Bridges  
 Executive Director

Attachments:           Petitioner's correspondence dated March 7, 2015  
                                   (which includes petition dated February 18, 2015, and other attachments)  
                                   Business Taxes Committee Formal Issue Paper No. 97-017

RF:RT:hp

cc:    Ms. Cynthia Bridges   MIC:73  
       Mr. Robert Tucker     MIC:82  
       Mr. Bradley Heller     MIC:82

**STATE BOARD OF EQUALIZATION**



BOARD APPROVED

At the March 26, 2015 Board Meeting

  
 Joann Richmond, Chief  
 Board Proceedings Division



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March 7, 2015

**VIA CERTIFIED MAIL RETURN RECEIPT REQUESTED**

Randy Ferris, Chief Counsel  
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450 N Street  
Sacramento, CA 95814-0083

Re: Notice and Demand, on Behalf of My Client Jenny Lee and a Class of Similarly Situated California Consumers, that the Board, *inter alia*, Refund the Excess Sales Tax Collected Pursuant to Regulation 1585

Dear Mr. Ferris,

On February 26, 2015, I received a letter (attached hereto as Exhibit A) from Richard Bennion, Board Regulations Coordinator, acknowledging the Board's Legal Department had received my client Jenny Lee's Petition to repeal Regulation 1585. Mr. Bennion also confirmed in the letter, and in a phone call to me, that the Board accepted our emailed offer (attached hereto as Exhibit B) of a conditional open-ended extension of time for the Board to set a hearing on the Petition, conditioned on that extension being revocable by Ms. Lee on 30 days written notice to the CBOE. Mr. Bennion further stated in the letter that regardless of the extension, the Board anticipates scheduling a hearing on the Petition during the Board's March 25-26 meeting. (The Petition is attached hereto as Exhibit C.)

Ms. Lee's Petition that the Board repeal Regulation 1585 is only one part of the relief that she seeks on behalf of herself and a class of similarly situated California consumers (the "Class") who have paid excess sales tax pursuant to Regulation 1585 on wireless telecommunications devices purchased as part of a "bundled transaction" where they were required to enter into a wireless services contract.<sup>1</sup>

---

<sup>1</sup> The Class paid such excess sales tax in a manner similar to Ms. Lee, as further described in the Petition. *I.e.*, pursuant to Regulation 1585 - and in violation of the California Revenue and Taxation Code - Class members were charged sales tax on a fictitious and inflated "unbundled" sales price for their devices, rather than on the lower price they actual paid for the devices at the point of sale.

March 7, 2015

Page 2

Ms. Lee also demands, on behalf of herself and the Class, that the Board do the following by March 26, 2015:

1. Ascertain that Regulation 1585 is unlawful and inconsistent with the California Revenue and Taxation Code;
2. Ascertain that the Class overpaid sales tax pursuant to Regulation 1585, in the amount of the difference between the sales tax they actually paid, and the lower sales tax that they would have paid if not for Regulation 1585;
3. Refund to the Class this excess sales tax collected by the Board pursuant to Regulation 1585; and
4. Direct retailers to refund to the Class any excess sales tax collected pursuant to Regulation 1585 which has not yet been submitted to the Board.

If the Board refuses to provide the demanded relief by March 26, 2015, Ms. Lee will file a class action lawsuit against the Board seeking declaratory relief, compensatory damages, restitution, and any other appropriate equitable relief.

Very truly yours,

A handwritten signature in black ink, appearing to read "Dan Hattis", with a long horizontal flourish extending to the right.

Daniel M. Hattis

Enclosures

cc: Jenny Lee  
Tony Tanke, Esq.  
Bradley Heller, Tax Counsel IV, Board of Equalization  
Richard Bennion, Regulations Coordinator, Board of Equalization

# **EXHIBIT A**



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](http://www.boe.ca.gov)

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

FIONA MA, CPA  
Second District, San Francisco

JEROME E. HORTON  
Third District, Los Angeles County

DIANE L. HARKEY  
Fourth District, Orange County

BETTY T. YEE  
State Controller

CYNTHIA BRIDGES  
Executive Director

February 26, 2015

Subject: Petition to Repeal Sales and Use Tax Regulation 1585

Dear Mr. Hattis,

On Monday, February 23, 2015, the Legal Department received your petition filed on behalf of Ms. Jenny Lee, pursuant to Government Code section 11340.6, requesting the repeal of California Code of Regulations, title 18, section (Regulation) 1585, *Cellular Telephones, Pagers, and Other Wireless Telecommunication Devices*.

We appreciate that Ms. Lee agreed to an open-ended extension of the 30-day period in Government Code section 11340.7 on the conditions that the extension is revocable by Ms. Lee on 30 days written notice to the Board and the Board is required to schedule a hearing on the petition within 30 days of Ms. Lee's notice of revocation, as indicated in your February 25, 2015, email.

Board staff anticipates scheduling a hearing on the petition during the Board's March 25-26, 2015, meeting in Sacramento. The public agenda notice (PAN) for that meeting will be available on the Board's website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days prior to that meeting. The PAN will include a link to a Chief Counsel Memorandum setting forth the Legal Department's recommendation regarding the petition.

If you have any questions or need more information, please contact Bradley Heller, Tax Counsel IV, at 916-323-3091.

Sincerely,

Richard Bennion  
Regulations Coordinator

# **EXHIBIT B**

**Subject:** Petition to Repeal Regulation 1585

**Date:** Wednesday, February 25, 2015 at 12:26:52 PM Pacific Standard Time

**From:** Daniel Hattis

**To:** Richard.Bennion@boe.ca.gov

**CC:** Kirill Devyatov

Dear Mr. Bennion,

It was good speaking with you this morning regarding consumer Jenny Lee's petition to repeal Regulation 1585.

Petitioner is willing to grant a conditional open-ended extension of time for the CBOE to set a hearing on the Petition, conditioned on that extension being revocable by Petitioner on 30 days written notice to the CBOE. This would require the CBOE to set the hearing within 30 days of Petitioner's notice of revocation. It would also insure there would be no inordinate delays in proceedings on the Petition.

Please confirm that the CBOE will agree to this condition where the extension is revocable on 30 days notice. If the CBOE will not agree, then Petitioner will not grant an extension for the CBOE to deny or set a hearing on the Petition pursuant to Gov't Code Section 11340.7.

Thank you,

Dan Hattis  
Hattis Law  
Office: 650.980.1990  
Mobile: 650.284.8495  
[www.hattislaw.com](http://www.hattislaw.com)

Confidential: This email may contain information protected by the attorney-client or work-product privilege. If you have received this email in error, please notify me immediately and then delete the message and any attachments.

# **EXHIBIT C**

BEFORE THE CALIFORNIA BOARD OF EQUALIZATION

In re Petition to the California Board of Equalization for Repeal of  
Cal. Code Regs. tit. 18, § 1585

---

**PETITION TO THE CALIFORNIA BOARD OF EQUALIZATION  
FOR REPEAL OF CAL. CODE REGS. TIT. 18, § 1585**

---

Daniel M. Hattis (State Bar No. 232141)  
Kirill M. Devyatov (State Bar No. 293106)  
HATTIS LAW  
2300 Geng Road, Suite 200  
Palo Alto, CA 94303  
Telephone: (650) 980-1990  
Facsimile: (650) 989-4189  
E-mail: dan@hattislaw.com  
kd@hattislaw.com

Attorneys for Petitioner Consumer Jenny Lee

## I. INTRODUCTION

Pursuant to Gov't Code § 11340.6, petitioner consumer Jenny Lee ("Petitioner") hereby petitions the California Board of Equalization ("CBOE") for the repeal of the Cal. Code Regs. tit. 18, §1585 ("Regulation 1585"). Petitioner purchased two mobile phones directly from AT&T, and was charged excessive sales tax on the phones at the point of sale. Pursuant to Regulation 1585, the sales tax was calculated not on the actual amount AT&T received for the transaction, but instead on a much higher fictitious "unbundled sales price," a term invented by the CBOE. The CBOE exceeded its authority in the promulgation of Regulation 1585 because the regulation is inconsistent with the California Revenue and Tax Code's requirement that all sales taxes are to be calculated based on the "gross receipts" retailers actually receive at the point of sale. *See Rev. & Tax. Code §§ 6012 and 6051.* The Regulation wrongly and unlawfully redefines "gross receipts" to include an imaginary, and arbitrary, dollar amount that is not actually received by the retailer for the transaction. Regulation 1585 must be repealed because the Administrative Procedure Act forbids the enforcement of regulations that exceed the authority granted by, or that are in conflict with, their purportedly authorizing statute. *See Gov't Code §§ 11342.1 and 11342.2.*

## II. INTEREST OF PETITIONER

Petitioner is an interested person because she paid excessive sales tax on mobile phones purchased from AT&T, where AT&T explicitly relied on Regulation 1585 in charging the tax. On December 27, 2012, Ms. Lee purchased an iPhone 5 for \$199.99 from AT&T's retail store located at 3251 20<sup>th</sup> Ave., Suite 240, San Francisco, CA. On December 18, 2013, Ms. Lee purchased an LG Optimus G Pro mobile phone for \$99.99 from the same store. *See receipts at Exhibit A.* Ms. Lee purchased each of the phones as part of a bundled transaction where she was required to sign a two-year contract with AT&T as her wireless carrier.

Pursuant to Regulation 1585, AT&T charged Ms. Lee sales tax of \$55.25 on the iPhone, and \$38.50 on the LG phone, based on what the CBOE calls the “unbundled sales price” of the phones. Ms. Lee would have paid sales tax of only \$17.00 on the iPhone, and \$8.75 on the LG phone, if the taxes had been based on the amount AT&T actually received, and she actually paid, at the point of sale. Ms. Lee overpaid sales tax on the transactions in the amount of \$68.00, which is the difference between the taxes she did pay (based on the fictitious \$649.99 and \$439.99 prices), and the taxes she would have paid if not for Regulation 1585 (based on the true \$199.99 and \$99.99 prices).

On November 17, 2014, Ms. Lee filed a BOE-101 Claim for Refund with the CBOE requesting that the CBOE: (1) refund the \$68.00 overpayment; (2) “ascertain” that Ms. Lee paid excessive sales tax; and (3) repeal Regulation 1585. *See* Exhibit B. On November 21, 2014, Ms. Lee received a written response from the CBOE denying her request. *See* Exhibit C. Ms. Lee is representative of millions of California consumers who have paid, and continue to pay, excessive sales taxes pursuant to the unlawful Regulation 1585.

### **III. ARGUMENT**

Gov’t Code § 11340.6 provides that any interested person may petition a California agency such as the CBOE to request the repeal of a regulation so long as the petition clearly and concisely states: “(a) The substance or nature of the regulation, amendment, or repeal requested, (b) The reason for the request, and (c) Reference to the authority of the state agency to take the action requested.” Petitioner hereby petitions the CBOE to repeal Regulation 1585.

#### **A. The substance or nature of the regulation, amendment, or repeal requested**

The CBOE wrongly promulgated in Regulation 1585 that the “gross receipts” from mobile phone sales be measured by the “unbundled sales price” of the phone, even when the actual price charged and received by the retailer is significantly lower. Rev. & Tax. Code §§ 6012(a) defines

“gross receipts” as the total amount of money received by the retailer for the transaction. In Regulation 1585, the CBOE acknowledges that sales tax must be applied “to the gross receipts from the retail sale of a wireless telecommunication device sold in a bundled transaction,” but then unilaterally and unlawfully specifies that the bundled transaction be “measured by the unbundled sales price of that device.” *See* Regulation 1585(b)(3).

Petitioner requests that the CBOE repeal Regulation 1585 because it is inconsistent with the plain meaning of the California Revenue and Taxation Code’s requirement that sales tax be calculated based on the “gross receipts” retailers receive at the point of sale. In the alternative to the CBOE repealing Regulation 1585 in its entirety, Ms. Lee petitions the CBOE to repeal Sections (a)(3-4), (b)(3-6), and (c) of the Regulation.

#### **B. The reason for the request**

Ms. Lee is representative of millions of California consumers who have paid, and continue to pay, excessive sales taxes pursuant to the unlawful Regulation 1585. The CBOE denied Ms. Lee’s BOE-101 Claim for Refund and told Ms. Lee that she has no standing to request a refund of sales tax from the CBOE, let alone to demand that the Regulation be repealed. *See* Exhibit B. This Gov’t Code § 11340.6 Petition provides the only avenue remaining to Ms. Lee, short of a lawsuit, to demand a refund and the repeal of Regulation 1585.

Whatever its motives, an administrative agency such as the CBOE has no discretion to promulgate a regulation that is inconsistent with its governing statutes. *See Terhune v. Superior Court*, 65 Cal. App. 4th 864 (1998); *Pulaski v. California Occupational Safety & Health Standards Board*, 75 Cal. App. 4th 1315, 1341 (1999); *Transworld Sys., Inc. v. County of Sonoma*, 78 Cal. App. 4th 713, 717 (2000). The Administrative Procedure Act forbids the enforcement of regulations that exceed the authority granted by, or that are in conflict with, their purportedly authorizing statute. Regulations must “be within the scope of authority conferred in

accordance with the standards prescribed by other provisions of law.” See Gov’t Code § 11342.1. Regulations that “alter or amend the [governing] statutes or enlarge or restrict the agency’s statutory power” are invalid. *California Beer & Wine Wholesalers Association v. Department of Alcoholic Beverage Control*, 201 Cal. App. 3d 100, 106-07 (1988).

The CBOE exceeded its authority when it promulgated Regulation 1585 because the regulation is inconsistent with the California Revenue and Taxation Code’s requirement that all sales taxes are to be calculated based on the “gross receipts” retailers actually receive at the point of sale. See Rev. & Tax. Code §§ 6012 and 6051. Contrary to the clear language in the Tax Code, Regulation 1585 unlawfully redefines “gross receipts” -- and does so only with regard to mobile phones and other wireless telecommunication devices -- to include an imaginary, and arbitrary, dollar amount that is not actually received by the retailer for the transaction.

**C. Authority of the CBOE to repeal Regulation 1585**

The CBOE has authority to promulgate regulations relating to the administration and enforcement of the Tax Code pursuant to Rev. & Tax. Code § 7051. Consequently, the CBOE also has authority to repeal such regulations.

**IV. DEMAND**

Pursuant to Gov’t Code §11340.7, the CBOE has thirty days from the receipt of this Petition to set a hearing on this Petition to repeal Regulation 1585 in its entirety (or in the alternative to repeal Sections (a)(3-4), (b)(3-6), and (c)), or to explain in writing why the CBOE denies the Petition. If the CBOE does not provide a response to this Petition, Ms. Lee will file a declaratory relief action pursuant to Gov’t Code §11350 to challenge Regulation 1585 as inconsistent with the Tax Code.

//

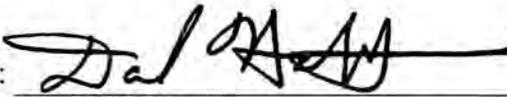
//

Petitioner looks forward to the CBOE's prompt response.

Dated: February 18, 2015

Respectfully submitted,

HATTIS LAW

By:   
Daniel M. Hattis

Daniel M. Hattis  
dan@hattislaw.com  
Kirill M. Devyatov  
kd@hattislaw.com  
HATTIS LAW  
2300 Geng Road, Suite 200  
Palo Alto, CA 94303  
Telephone: (650) 980-1990

*Attorneys for Petitioner Consumer Jenny Lee*

EXHIBIT A to Petition



San Francisco Stonestown Retail Store  
3251 20th Ave, Suite 240, AT&T Store  
San Francisco, CA 94132  
(415) 564-2171  
Store No. S192 Register No. 41

Customer:  
JENNY LEE  
415-235-5851 (T)  
69300 PHO IPHONE 5 16GB BLK 199.99  
SER. NO. 013431001390824  
Taxable Unit Value 649.99  
ADDED 24 Months  
CHANGED SIM 8901403255422569328  
CHANGED TIME 013431001390824  
ADDED DATA PLAN UNL LTE TP  
ACCOUNT NOTE 415-235-5851

Customer:  
JENNY LEE  
415-288-3200 (T)  
DELETED IPHONE MSG UNL  
Customer:  
JENNY LEE  
415-388-7721 (T)  
ADDED Family Messaging UNL with

SUBTOTAL 199.99  
TAX 55.25  
TOTAL AMOUNT DUE 255.24  
MEMBER SAVINGS - \$450.00  
CORPORATE ACCESSORY DISCOUNT \$0.00  
AMERICAN EXPRESS TENDERED 255.24  
Acct. No. XXXXXXXXXXX1007  
Auth No. 509970

CHANGE DUE 0.00

YOUR TOTAL SAVINGS \$450.00

American Express  
Acct. No. XXXXXXXXXXX1007  
Auth No. 509970  
AMOUNT \$255.24

I HAVE RECEIVED GOODS AND SERVICES IN THE ABOVE AMOUNT

SIGN X \_\_\_\_\_

CASHIER: STEPHANIE T



\*XST922AD7VSL9\*

11/27/2012 13:08:27

STORE COPY

\*\*\*\*\*  
THANK YOU FOR CHOOSING AT&T!  
\*\*\*\*\*

NEED HELP?

Get 24 x 7 support for all your AT&T services at att.com/support

RETURN INFORMATION

Return a restocking fee policy on back  
Pursuant to California Sales Tax  
Regulation 1586, tax on devices sold with  
services are calculated based on the no  
cost pricing.

\*\*\*\*\*  
THANK YOU FOR CHOOSING AT&T!  
\*\*\*\*\*

NEED HELP?

Get 24 x 7 support for all your AT&T services at att.com/support



San Francisco Stonestown Retail Store  
 3251 20th Ave, Suite 240, AT&T Store  
 San Francisco, CA 94132  
 (415) 564-2171

Store No. S192  
 OM Tablet No. 17

Customer:  
 JENNY LEE  
 415-308-7721 (T)

6053A PHO LGE OPT G PRO E980 99.99  
 SER. NO. 013520002278085  
 Taxable Unit Value 439.99  
 40954 SIM UNCD-G 3FF MICRO 0.00  
 SER. NO. 89014104276557689740  
 Taxable Unit Value 0.00  
 76304 DECLINED INSURANCE 0.00  
 1 @ 0.00 No Discount Available  
 ADDED 24 Months  
 CHANGED SIM# 89014104276557589740  
 CHANGED LINE# 013520002278085  
 ADDED Device 306 per Smartphone  
 ACCOUNT NOTE 415-308-7721

SUBTOTAL 99.99  
 TAX 38.50  
 TOTAL AMOUNT DUE 138.49  
 COMMITMENT SAVINGS - \$340.00  
 CORPORATE ACCESSORY DISCOUNT \$0.00  
 VISA TENDERED 138.49  
 Acct No. XXXXXXXXXXXX5056  
 Auth No. 052158  
 CHANGE DUE 0.00  
 YOUR TOTAL SAVINGS \$340.00

Visa  
 Acct No. XXXXXXXXXXXX5056  
 AUTH No. 052158  
 AMOUNT \$138.49

I HAVE RECEIVED GOODS AND  
 SERVICES IN THE ABOVE AMOUNT

CASHIER: VINCENT W



\* X S T 9 2 1 F F 5 B 3 F 9 \*

NOV 18 / 2018 18:58:46

STOCK COPY

\*\*\*\*\*

THANK YOU FOR CHOOSING AT&T!

\*\*\*\*\*

NEED HELP?

Get 24 x 7 support for all your  
 AT&T services at att.com/support

RETURN INFORMATION

Return & restocking fee policy on back  
 Pursuant to California Sales Tax  
 Regulation 1586, tax on devices sold with  
 service are calculated based on the no  
 commit pricing.

\*\*\*\*\*

THANK YOU FOR CHOOSING AT&T!

\*\*\*\*\*

NEED HELP?

Get 24 x 7 support for all your  
 AT&T services at att.com/support

EXHIBIT B to Petition  
**HATTIS LAW**

Daniel M. Hattis, Esq.  
2300 Geng Road, Suite 200  
Palo Alto, CA 94303  
dan@hattislaw.com  
T – 650.980.1990  
F – 650.989.4189

November 17, 2014

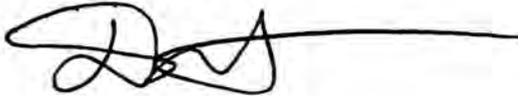
State Board of Equalization  
P.O. Box 942879  
Sacramento, CA 94279

Re: My Client: Jenny Lee  
BOE-101 Claim for Refund  
Overpayment of Sales Tax on Mobile Phone

To Whom It May Concern:

Please find enclosed my above-referenced client's claim for a refund of \$68.00 for overpaid sales tax on mobile phones purchased on December 27, 2012 and December 18, 2013.

Very truly yours,



Daniel M. Hattis

Enclosures: BOE-101, Exhibit A, Copy of Sales Receipts

**CLAIM FOR REFUND OR CREDIT**

(Instructions on back)

NAME OF TAXPAYER(S) OR FEEPAyer(S)

Jenny Lee

TAXPAYER'S OR FEEPAyer'S ACCOUNT NO.

GENERAL PARTNER (if applicable)

TAXPAYER'S OR FEEPAyer'S SOCIAL SECURITY NUMBER(S)\* OR FEDERAL EMPLOYER IDENTIFICATION NUMBER

[REDACTED]

According to

- Chapter 7, Article 1, of the California Sales and Use Tax Law, and where applicable, Uniform Local Sales and Use Tax Ordinances and the Transit District Transactions (Sales) and Use Tax Ordinances, or
- Chapter 6, Article 1, of the California Use Fuel Tax Law, or
- Chapter 8, Article 1 and 2, of the Diesel Fuel Tax Law,
- Other \_\_\_\_\_ (please specify the applicable tax law or fee program)

the undersigned hereby makes claim for refund or credit of \$ 68.00 (may be left blank), or such other amounts as may be established, in tax, interest and penalty in connection with:

- Return(s) filed for the period \_\_\_\_\_ to \_\_\_\_\_
- Determination(s) dated \_\_\_\_\_ and paid \_\_\_\_\_
- Other (describe fully)

Ms. Lee's overpayment of mobile phone sales taxes paid on 12/27/12 and 12/18/13, because CBOE Regulation 1585, upon which the AT&T relied in charging her sales tax on inflated and fictitious transaction amounts, is unlawful.

The overpayment described above was caused by

See attached "Exhibit A"

Supporting Documentation:

- is attached
- will be provided upon request

BUSINESS NAME

SIGNED BY 		DATE SIGNED 11/17/2014	
PRINT NAME OF SIGNATORY Daniel M. Hattis		CONTACT PERSON (if other than signatory)	
TITLE OR POSITION Attorney for Ms. Lee	TELEPHONE NUMBER ( 650 ) 980-1990	TITLE OR POSITION OF CONTACT PERSON	TELEPHONE NUMBER ( )

Credit interest is available under certain circumstances. If you would like to be considered for credit interest, please check here.

\*See BOE-324-GEN, Privacy Notice, regarding disclosure of the applicable social security number.

<b>FOR BOE USE ONLY</b>
Case ID No. _____

**EXHIBIT A**  
**Form BOE-101**  
**Jenny Lee, SSN [REDACTED]**

On December 27, 2012, Ms. Lee purchased an iPhone 5 mobile phone from AT&T's retail store located at 3251 20<sup>th</sup> Ave., Suite 240, San Francisco, CA, for \$199.99. On December 18, 2013, Ms. Lee purchased an LG Optimus G Pro mobile phone from the same store for \$99.99. *See* attached receipts. Ms. Lee purchased each of the mobile phones as part of a bundled transaction where she was required to sign a two-year contract with AT&T as her wireless carrier.

Pursuant to California Board of Equalization ("CBOE") Regulation 1585, AT&T charged Ms. Lee sales tax of \$55.25 on the iPhone 5, and \$38.50 on the LG phone, based on what the CBOE calls the "unbundled sales price" of the phones. Ms. Lee would have paid sales tax of only \$17.00 on the iPhone 5, and \$8.75 on the LG phone, if the taxes had been based on the amount AT&T actually received, and she actually paid, at the point of sale. Ms. Lee believes she overpaid sales tax on the transactions and demands a refund in the amount of \$68.00, which is the difference between the taxes she actually paid (based on the fictitious \$649.99 and \$439.99 prices), and the taxes she should have paid (based on the true \$199.99 and \$99.99 prices she was actually charged for the phones).

Ms. Lee is entitled to the refund because Regulation 1585, which AT&T explicitly relied upon in charging the excess tax, is unlawful. Regulation 1585 directly conflicts with the California Revenue and Tax Code's ("Tax Code") explicit requirement that sales taxes be limited to the "gross receipts" retailers receive at the point of sale. *See* Rev. & Tax. Code § 6051. The Tax Code defines gross receipts as the total amount of money received by the retailer for the transaction. *Id.* § 6012. Under Regulation 1585, the CBOE wrongly redefined "gross receipts" with regard to mobile phone sales to be measured by the "unbundled sales price" of the phone (*e.g.*, \$649.99), even when the actual price paid to the retailer is significantly lower (*e.g.*, \$199.99). Under Regulation 1585 retailers are directed to pay (and are permitted to pass through to consumers) taxes on entirely imaginary transaction amounts never actually paid to the retailers, in direct violation of Rev. & Tax. Code §§ 6051 and 6012.

CBOE exceeded its authority in creating Regulation 1585. The CBOE may only "prescribe, adopt, and enforce rules and regulations relating to the administration and enforcement" of the Tax Code. *Id.* § 7051. The CBOE cannot invent new taxes out of whole cloth that directly conflict with the clear language of the Tax Code itself.

Based on the foregoing, Ms. Lee demands a refund from the CBOE in the amount of \$68.00, which is the excess sales tax she paid, and the CBOE received, under the unlawful Regulation 1585 sales tax scheme. Ms. Lee demands that pursuant to Rev. & Tax. Code § 6901.5, the CBOE "ascertain" that she paid sales taxes computed on amounts (*i.e.*, \$649.99 and \$439.99) that were in excess of the taxable amounts (*i.e.*, \$199.99 and \$99.99). She further demands that the CBOE repeal Regulation 1585.

# EXHIBIT C to Petition



STATE OF CALIFORNIA

## STATE BOARD OF EQUALIZATION

450 N STREET, SACRAMENTO, CALIFORNIA  
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0039  
TELEPHONE (916) 324-3017  
FAX (916) 445-2249 OR 324-0147  
Roslyn.Nera@boe.ca.gov

BETTY T. YEE

First District, San Francisco

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

MICHELLE STEEL  
Third District, Orange County

JEROME E. HORTON  
Fourth District, Los Angeles

JOHN CHIANG  
State Controller

CYNTHIA BRIDGES  
Executive Director

November 20, 2014

Daniel M. Hattis, Esq.  
2300 Geng Rd., Suite 200  
Palo Alto, CA 94303

Re: Jenny Lee  
Request for Refund  
Postmarked: November 17, 2014  
Received: November 19, 2014

Dear Claimant:

Your claim for refund postmark dated November 17, 2014 and received in our office on November 19, 2014; in which you request a refund of \$68.00 for sales tax paid to AT&T has been referred to this office for consideration.

Under California law, a refund of an overpayment of sales tax may be made only to the firm or individual who paid the tax to this Board. Your recourse, therefore, is to contact AT&T. They, in turn, may file a claim for refund with us, supported by the proper documentation. Any refund due would be issued to the seller with the provision that it passed on to you.

We regret that we cannot be of direct assistance to you in this matter.

Thank you for your cooperation.

Sincerely,

Roslyn D. Nera  
Senior Tax Auditor

Audit Determination & Refund Section

Issue Paper Number 97-017



BOARD OF EQUALIZATION  
**KEY AGENCY ISSUE**

- Board Meeting
- Business Taxes Committee
- Customer Services Committee
- Legislative Committee
- Property Tax Committee
- Other

---

## 97-017

### Regulation 1585 - Cellular Telephones, Pagers, and Other Telecommunications Devices

#### I. Issue

Should the Board authorize publication of proposed Sales and Use Tax Regulation 1585, *Cellular Telephones, Pagers, and Other Telecommunications Devices*?

#### II. Staff Recommendation

Staff recommends the Board authorize publication of the attached proposed new Regulation 1585, with minor revisions as suggested by industry and noted within section (V), subdivision (A).

#### III. Other Alternative(s) Considered

Not applicable.

#### **IV. Background**

The wireless telecommunications industry is a rapidly changing industry, existing in a fluctuating and capricious market place. Consequently, marketing and retail pricing strategies that contradict conventional and customary retail practices are rampant within this industry, resulting in widespread, below cost sales of cellular telephones and paging devices. The practice is facilitated by the direct payment of rebates and/or commissions, by the wireless telecommunications service provider, to the retailers who couple the respective contract for utility service with the sales of the wireless telecommunications devices.

When a retailer of cellular telephones requires that the purchaser obtain wireless telecommunications service (bundles) from a particular service provider who will then pay the retailer a commission, the Board regards the commissions as part of the taxable gross receipts from the retailer's sale of the telecommunications device. Since the purchaser presumably has a contract with and pays the service provider for the wireless telecommunications service, the payment from the customer to the service provider is not included in the measure of tax. However, the rebates and/or commissions received by the retailer from the service provider are not for exempt wireless telecommunications service. Consequently, the indirect reimbursement for the wireless telecommunications devices in addition to the amount specifically charged the customer on the sales agreement is required to be included in the measure of tax.

Under Revenue and Taxation Code section 6012, gross receipts received from the retail sale of tangible personal property in this state are subject to tax. Taxable gross receipts include the total sales price, valued in money, whether received in money or otherwise, with no deduction for charges, expenses, or services that are part of the sale. Normally, a service is regarded as part of the sale if the purchaser cannot obtain the tangible personal property without also obtaining the service, or cannot obtain the tangible personal property at the same price without the service.

Although below cost pricing was occurring in the industry as early as 1991, retailers did not bring the issue before staff until sometime in 1993. Apparently, the affected retailers believed the issue was handled through legislation introduced in 1992. In an effort by the Legislature to deal with below cost pricing, Assembly Bill 275 (Stats 1992, Ch. 542) was introduced and subsequently added section 17026.1 to the California Business and Professions Code (B&P). The bill specifically addressed the issue of offering discounts to customers who activated service, and the respective commissions that were paid to the retailers upon such activation. In doing so, it appeared that the Legislature provided the necessary provisions to prevent extensive below cost pricing in the industry.

Operative January 1, 1994, section 17026.1 of the B&P Code provides that:

- (b) In each retail location, all retailers of cellular telephones shall post a large conspicuous sign...that states the following: "Activation of any cellular telephone is not required and the advertised price of any cellular phone is not

contingent upon activation, acceptance, or denial of cellular service by any cellular provider.”

Section 17026.1(a)(2) of the Business and Professions Codes states that:

“...providers of cellular service shall be permitted to sell cellular telephones below cost, provided that sales below cost are a good faith endeavor to meet the legal market prices of competitors in the same locality or trade area.”

Further, section 17026.1(a)(1) provides that:

“...commissions or rebates regularly earned by the retailers of cellular telephones may be used to reduce cost, provided, that in no event shall the reduction exceed the greater of the following: (A) Ten percent of cost, ...or (B) Twenty dollars (\$20).”

Thus, a cellular telephone retailer was not expected to place a specific written stipulation on a customer with respect to coupling an activation policy as a prerequisite for the purchase of cellular equipment. Nevertheless, in the last four to five years staff has been responding to numerous complaints and concerns of a number of retailers who have been negatively impacted by the competitive selling practice of pricing wireless telecommunications devices significantly below cost. In 1993, such pricing was as much as 40 to 50% below cost. Retailers expressing their concerns believed that the Board should administer fair trade provisions with respect to the pricing of wireless telecommunications devices, since many retailers appeared to be ignoring the provisions found within the B&P Code.

New marketing and pricing strategies continued to be introduced and practiced within the industry. Staff continued to receive inquiries from retailers concerned with the industry's frequent below cost pricing practices, and what many continued to refer to as “unfair” competition. Throughout 1994 and into 1995, staff continued to track the situation, and maintained its contact with industry representatives. Until the beginning of 1995, extensive below cost pricing appeared to be confined to a limited number of retailers within the industry.

However, in April of 1995, things changed within the wireless telecommunications industry. On April 5, 1995, the California Public Utilities Commission (PUC) approved tying cellular telephone sales with specific wireless telecommunications service and, in doing so, reversed their long standing ban against “bundling” (the practice of coupling wireless device sales with the respective utility service contract) in the industry. This caused confusion on the part of many retailers, resulting in telephone calls to staff and rumors that the PUC would reverse their decision. Apparently, retailers believed the PUC decision was in direct conflict with B&P Code section 17026.1(c) that provides that:

“No retailer of cellular telephones shall refuse to sell a cellular telephone to any customer solely on the basis of the customer's refusal to activate the telephone with the provider of cellular service for whom the retailer is an agent.... The

intent of this subdivision is to reaffirm the Legislature's support for the Public Utilities Commission's policy that makes illegal the act, or practice of "bundling," as defined and described in relevant decisions and orders of the commission."

Since the PUC decision did not result in a like reversal of B&P Code section 17026.1(c), retailers believed that the Board could enforce the B&P Code and, as such, assist in invalidating the PUC decision. However, even though the respective B&P Code provisions directly related to the "bundling" issue, the statutes continue to be beyond the administrative province of the Board. Additionally, subdivision (d) of the B&P Code provides what can be deemed a disclaimer against any provisions of the B&P Code that may conflict with the rules, regulations, or orders promulgated or issued by the PUC. Consequently, the PUC stance on "bundling" opened the door for new and inventive marketing strategies within the wireless telecommunications industry, resulting in extensive below cost pricing, with such "steep" discounts being contingent on the customers' activation with a related service provider.

With the "steep" discounts and required activation (bundling), and the fact that the B&P Code did not invalidate the PUC decision, came confusion over what portions of the retailers' receipts were included in taxable measure. Since retailers are generally able to recoup such discounts through the commissions and/or rebates paid by the service providers, and such activation is a condition of the sale, staff regards the commissions as part of the gross receipts received for the retailers' sale of the wireless device. Accordingly, this presented an additional dilemma for the retailers, industry, and staff.

On April 24, 1997, staff met with retailers and cellular officials to discuss the application of tax to bundled transactions. During the meeting, the retailers expressed concern with the administrative difficulty of tracking and properly reporting the commission component of gross receipts received on wireless device transactions. For administrative ease, the retailers advocated reporting tax measured by the price at which the device is sold to customers who do not contract for the wireless telecommunications service. Such price is commonly referred to as the "unbundled" or "unactivated" price. The service providers also agreed to this pricing structure as they did not want two standards giving them a competitive advantage over the retailers. Staff agreed to examine documents related to these types of cellular transactions and determine the feasibility of the industry proposal. Considering the results of staff's analysis, staff recommended that retailers be allowed to report tax measured by the unbundled retail selling price. Due to the unique nature of this reporting basis, staff has continued to work with and maintain contact with industry representatives to ensure clarification concerning this matter and to enlist their assistance in drafting the proposed regulation.

To summarize, present day sales of wireless telecommunications devices at prices as low as 90% below cost are occurring throughout the wireless telecommunications industry. In many instances, the devices are offered free of charge. Whatever the pricing strategy, the "steep" discounts are almost always contingent upon activation with a specific wireless telecommunications service provider. In contrast to past practices, small and

large retailers alike are practicing today's below cost pricing of analog cellular telephones and various types of pagers.

Considering the transitory nature of the industry's marketing and pricing strategies and the tendency for the various wireless devices to become outdated and replaced with "smaller and better" models within a short period of time, the regulation must provide specific statutory interpretations that conform to not only the governing provisions of section 6012, but other statutory laws within the Revenue and Taxation Code as well. Additionally, the draft must be flexible enough to provide for the application of tax to the sales of devices occurring in today's market and those that took place in the past, as well as those expected to occur in the future. Although the marketing strategies of the industry are somewhat unique to that specific industry, the premise upon which the regulation's statutory authority is based is not unique. It is the principle upon which the taxability of all retail sales is firmly established.

Consequently, staff is endeavoring to provide guidance to the industry, while attempting to effectively administer and implement the applicable provisions of the law. To do so, staff has written proposed regulation 1585 with the input and assistance of industry representatives. Accordingly, staff has had many telephone conversations with industry representatives and received feedback and suggestions concerning the drafting of the regulation.

Proposed Regulation 1585 was designed primarily to address the application of tax in two situations: 1) the sale of a cellular telephone or pager in a bundled transaction; and 2) the sale of a cellular telephone or pager requiring activation exclusively with a particular utility service provider. Although industry's input has been invaluable, staff disagrees with some of industry's proposals (attachment 2) to the extent they depart from either of these objectives. Staff's thoughts on industry's proposed changes to the proposed draft of Regulation 1585 are provided within the text of the recommendation portion of this paper.

## **V. Staff Recommendation**

### **A. Recommendation.**

Staff recommends the following specific provisions of proposed new regulation 1585. Recommendations discuss industry's input and, when appropriate, recommend inclusion of same.

- Subdivision (a). Subdivision (a) provides the following definitions to provide the understanding and clarity necessary to interpret, implement, and make certain Section 6012.

1. Subdivision (a)(1) defines the term wireless telecommunications device, the sales of which the provisions of the proposed regulation relate. "Wireless telecommunications device" is meant to include portable wireless communication devices such as cellular telephones and pagers requiring activation by a utility service provider in order to function. Industry proposes to change the term of "utility service provider" to "wireless telecommunications service provider." Staff agrees with the proposed change.
2. Subdivision (a)(2) defines the term "utility service provider" to mean a utility regulated by the Public Utilities Commission or the Common Carrier Bureau of the Federal Communications Commission, which offers and/or provides wireless utility service. Industry proposes to define a wireless telecommunications service provider as "a provider of commercial mobile radio services as defined in ...47 CFR 20.3." Staff cannot agree with this proposal for the following reasons: 1) Proposed Regulation 1585 would be subject to definitional changes that may occur by way of modification to the CFR. For example, if 47 CFR 20.3 was modified by Congress or the FCC, proposed Regulation 1585 would also be changed; and 2) 47 CFR 20.3 does not appear to cover all aspects of wireless telecommunications as contemplated by proposed Regulation 1585.
3. Subdivision (a)(3) defines the term "bundled transaction" as the retail sale of a wireless telecommunications device requiring the retailer's customer to contract with a utility service provider as a condition of that sale. The subdivision interprets, implements, and makes certain Section 6012. Industry proposes to add "activate or" to subdivision (a)(3). With the suggested additional wording, subdivision (a)(3) to read as follows: "The retail sale of a wireless telecommunications device requires the retailer's customer to activate or contract with a wireless telecommunications utility service provider for utility service as a condition of that sale."... Staff accepts the proposed additional language.
4. Subdivision (a)(4) interprets, implements and makes certain section 6012. Industry proposes elimination of language making the unbundled sales price equal to the fair retail selling price consistent with industry's usual and customary retail pricing practices. Staff believes this language should be left in, but that it could be modified to reflect the pricing practices of local retailers. Staff and industry do agree that the regulation should address the sale of discontinued and obsolete merchandise. Staff believes that industry's "lined-out" language should be replaced with: "the unbundled sales price of a wireless telecommunications device shall equal the fair retail selling price of that device and shall be consistent with the usual and customary retail pricing practices of other local retailers for the type of device sold. The unbundled sales price of an obsolete wireless telecommunications device shall equal the

actual selling price of that device.” Staff also recommends that the words “would sell” on line one be changed to “has sold.”

5. Subdivision (a)(5) interprets section 6012 as it pertains to exclusive wireless service provider transactions. Industry proposes that the name for these types of transactions be changed to “Consignment Transactions” and that language defining these transactions be copied from a portion of industry’s proposed revisions to subdivision (b)(3). Staff disagrees. These types of transactions are not always consignment sales in that the person transferring the device to the end-use customer often has title to the device. Industry’s proposed definition also fails to recognize that the end-use customer is required to contract exclusively with a particular service provider as a condition of purchasing the wireless device. Staff does believe that the term “Carrier Restricted Transaction” should be replaced with the term “Exclusive Service Provider Transactions” for clarification purposes.
  6. Subdivision (a)(6) defines retail utilities transactions as the combined retail sale of a wireless telecommunications device and the respective service by a single retailer. Industry proposes a different name for the definition of this type of transaction. Staff remains of the opinion that the word “utilities” is necessary for describing these types of transactions.
- Subdivision (b). Interprets and makes certain the application of tax to these types of transactions.
    1. Subdivision (b)(1) interprets and makes certain section 6012.
    2. Subdivision (b)(2) interprets and makes certain section 6012. See subdivision (a)(6) for staff’s response to industry’s proposals concerning this subdivision.
    3. Subdivision (b)(3) interprets, implements, and makes certain section 6012. As for industry’s proposed changes, industry continues to classify all transactions as consignment sales and proposes that two separate entities pay tax measured by a portion of the total amount collected from an end-use customer. (This would also mean that two separate entities would attempt to collect tax reimbursement from a single, end-use customer.) Staff disagrees with this proposal. As set forth in staff’s response to subdivision (a)(5), not all transactions within this category are consignment sales. Staff further believes that allowing two different entities to report tax on a portion of the total amount collected from an end-use customer would create consumer protection problems as well as administrative difficulties in performing audits. One alternative is to allow the person deemed the retailer for the transaction to report tax measured by the entire unbundled sales price of the wireless telecommunications device.

4. Subdivision (b)(4) interprets, implements, and makes certain section 6012. Staff believes that industry no longer objects to the provisions of this subdivision. However, one other interested party has suggested that language be added to clarify the meaning of electronic modification. Although staff does not object to inclusion of such clarification, it may not be considered necessary. Industry and staff are in agreement regarding the difference between the electronic modification of a telecommunications device and the act of electronically activating such a device.
- Subdivisions (c) and (c)(1) implement and make certain the provisions of Regulation 1642.
    1. Subdivision (c)(2) implements and makes certain the provisions of Regulation 1642 as they apply to charge-backs by the wireless telecommunications service provider to the retailer. Industry proposes that the words “a payment or rebate” be substituted with the word “consideration.” Staff disagrees with this proposal. The word consideration is a technical legal term, with a particular meaning and consequences. The regulation uses terms commonly understood in the business community, in accordance with rulemaking requirements.
    2. Subdivision (c)(3) implements and makes certain the provisions of Regulation 1642 as they apply to charge-backs concerning retail utility transactions.

**B. Pros.**

This proposed new regulation is necessary to provide guidance and clarification to that part of the public affected by it.

**C. Cons.**

There appear to be no negative aspects of the recommendation.

**D. Statutory or Regulatory Change.**

As recommended, it is suggested that proposed Regulation 1585 be published and adopted.

**E. Administrative Impact.**

The adoption and publication of proposed Regulation 1585 will provide staff with the regulatory authority to continue to implement current policies and procedures.

**F. Fiscal Impact.**

1. Cost Impact.

Staff is currently implementing provisions. Any associated costs are absorbable.

2. Revenue Impact.

Since the provisions of the regulation reflect current policy, a revenue impact is not expected.

**G. Taxpayer/Customer Impact.**

Taxpayers will be better informed on the proper application of tax and, as such, better able to accurately report the tax due.

**H. Critical Time Frame.**

As the transactions addressed within the proposed regulation are already occurring, guidance needs to be provided as soon as possible.

**VI. Alternative 1**

Not applicable.

Prepared by: Sales and Use Tax Department, Audit Evaluation, Planning, and Settlement Section.

Current as of December 17, 1997.

**Regulation 1585. CELLULAR TELEPHONES, PAGERS, AND OTHER WIRELESS TELECOMMUNICATION DEVICES.**

**(a) DEFINITIONS.**

**(1) WIRELESS TELECOMMUNICATION DEVICE.** A portable communication device such as a cellular telephone or pager requiring activation by a utility service provider or seller of utility services in order to send, receive, or send and receive transmissions via a network of wireless transmitters throughout multiple service areas, or otherwise.

**(2) UTILITY SERVICE PROVIDER.** A utility regulated by the Public Utilities Commission or the Common Carrier Bureau of the Federal Communications Commission which offers or provides wireless communication or paging services.

**(3) BUNDLED TRANSACTION.** The retail sale of a wireless telecommunication device which requires the retailer's customer to contract with a utility service provider for utility service as a condition of that sale. A transaction is a bundled transaction within the meaning of this section without regard to the method in which the price is stated to the customer. Also, it is immaterial whether the wireless telecommunication device and utility service are sold for a single price or are separately itemized in the context of a sale or on a sales invoice.

**(4) UNBUNDLED SALES PRICE.** The price at which a retailer would sell a specific wireless telecommunication device to a customer who is not required to activate or contract with a utility service provider for utility service as a condition of that sale. The unbundled sales price of a wireless telecommunication device shall equal the fair retail selling price of that device and shall be consistent with the industry's usual and customary retail pricing practices for the type of device sold.

**(5) CARRIER RESTRICTED TRANSACTION.** The sale of a wireless telecommunication device which requires the customer purchasing the device to contract with one specific utility service provider for utility service as a condition of that sale. The customer purchasing the wireless telecommunication device is generally required to pay a predetermined fee to the utility service provider in the event that customer fails to obtain utility service from that utility service provider. The person providing the wireless telecommunication device to the customer does not receive a rebate or payment for obtaining the customer's contract with that utility service provider.

**(6) RETAIL UTILITIES TRANSACTION.** The combined retail sale of a wireless telecommunication device and utility service by a single retailer not affiliated with, or a part of, a utility service provider. The retailer of a wireless telecommunication device purchases utility service from a utility service provider for sale directly to its customer. Customers are required to contract for utility service from the retailer upon the sale of a wireless telecommunication device to that customer. The sales price listed on the customer's sales receipt or invoice for the wireless telecommunication device may or may not be below the retailer's acquisition cost of that device. The customer continues to pay the retailer for utility service throughout the duration of the utility service contract.

CELLULAR TELEPHONES, PAGERS, AND OTHER  
WIRELESS TELECOMMUNICATION DEVICES.

(b) APPLICATION OF TAX.

(1) IN GENERAL. Tax applies to the gross receipts from the retail sale of a wireless telecommunication device. The retailer of the wireless telecommunication device is required to report and pay the tax.

(2) BUNDLED TRANSACTIONS AND RETAIL UTILITIES TRANSACTIONS. Tax applies to the gross receipts from the retail sale of a wireless telecommunication device sold in a bundled transaction or in a retail utilities transaction, measured by the unbundled sales price of that device. Tax applies to the unbundled sales price whether the wireless telecommunication device and utility service are sold for a single price or are separately itemized in the context of a sale or on a sales invoice. The retailer of the wireless telecommunication device is required to report and pay tax measured by the unbundled sales price of the device and may collect tax or tax reimbursement from its customer measured by the unbundled sales price. Tax does not apply to the charges in excess of the unbundled sales price made for telecommunication services.

(3) CARRIER RESTRICTED TRANSACTIONS. The utility service provider is generally regarded as the retailer of the wireless telecommunication device notwithstanding any agreement or contractual obligation between the utility service provider and the person or entity providing the device to an end-use customer. Where the utility service provider reimburses or rebates money to a separate person or entity, that person or entity receiving the reimbursement or rebate is regarded as the retailer of the wireless telecommunication device. In either event, the person or entity regarded as the retailer of the wireless telecommunication device owes tax to the Board measured by the unbundled sales price of that device. The retailer may not collect tax or tax reimbursement from either the end-use customer or the person selling the device to the end-use customer.

(4) ACTIVATION FEES. Tax does not apply to a one-time charge for activating a new wireless telecommunication device with, or on behalf of, a utility service provider where the charge is separately stated and is not for the electronic or physical modification of the device in order for it to function within a utility service provider's service network. A one-time charge for activating a wireless telecommunication device is subject to tax if the activation consists of the physical or electronic modification or fabrication of a wireless telecommunication device in order for the device to function within a utility service provider's service network. The person collecting this fee is required to report and pay tax on that amount. Any subsequent charge for the physical or electronic modification or fabrication of that device which changes the customer's telephone number or which allows that customer to utilize a different utility service provider is subject to tax as set forth in Regulation 1546 (18 CCR 1546).

CELLULAR TELEPHONES, PAGERS, AND OTHER  
WIRELESS TELECOMMUNICATION DEVICES.

(c) BAD DEBT DEDUCTIONS.

(1) IN GENERAL. The provisions of Regulation 1642, "Bad Debts" (18 CCR 1642), apply to retailers making sales of wireless telecommunication devices pursuant to subdivision (b)(1).

(2) CHARGE-BACKS TO THE RETAILER. Retailers reporting tax measured by the unbundled sales price of a wireless telecommunication device may take a bad debt deduction pursuant to Regulation 1642 when a payment or rebate from a utility service provider is charged-back to the retailer based on a customer's termination of its contract with the utility service provider before the date specified in the utility service contract. The amount of bad debt deduction claimed by a retailer may not exceed the difference between the gross receipts on which tax was reported and paid by the retailer, and the total amount collected and retained by the retailer from the sale of the wireless telecommunication device excluding any amounts collected from the customer as tax or tax reimbursement. Any tax or tax reimbursement collected by the retailer on the amount of bad debt deduction claimed by the retailer constitutes excess tax reimbursement and must be returned to the customer or paid to the Board unless the customer and retailer agree that this amount may be applied toward the amounts owed by the customer on the debt. The customer and retailer will be regarded as having agreed to the application of any excess tax reimbursement to the customer's debt where the retailer's books reflect both the debt owed by the customer and the corresponding credit for excess tax reimbursement.

(3) RETAIL UTILITY TRANSACTIONS. Retailers of wireless telecommunication devices sold in a retail utilities transaction may take a bad debt deduction pursuant to Regulation 1642 when a customer terminates its utility service contract with the retailer before the date specified in the utility service contract. The amount of bad debt deduction claimed by a retailer may not exceed the difference between the gross receipts on which tax was reported and paid by the retailer, and the total amount collected and retained by the retailer in connection with the sale of the wireless telecommunication device excluding any amounts collected from the customer as tax or tax reimbursement. The amount collected from the customer on the retail utility transaction shall be allocated among the total amount collected for both the wireless telecommunication device and utility service by dividing the unbundled sales price by the total amount the retailer would have collected if the customer fully performed under the terms of the utility service contract, and then multiplying that amount by the total amount collected by the retailer to date.

Any tax or tax reimbursement collected by the retailer on the amount of bad debt deduction claimed by the retailer constitutes excess tax reimbursement and must be returned to the customer or paid to the Board unless the customer and retailer agree that this amount may be applied toward the amounts owed by the customer on the bad debt. The customer and retailer will be regarded as having agreed to the application of any excess tax reimbursement to the customer's debt where the retailer's books reflect both the debt owed by the customer and the corresponding credit for excess tax reimbursement.



**Regulation 1585. CELLULAR TELEPHONES, PAGERS, AND OTHER  
WIRELESS TELECOMMUNICATIONS DEVICES**

(a) DEFINITIONS.

(1) **WIRELESS TELECOMMUNICATIONS DEVICE.** A portable communications device such as a cellular telephone or pager requiring activation by a **wireless telecommunications utility** service provider or seller of utility services in order to send, receive, or send and receive transmissions via a network of wireless transmitters throughout multiple service areas, or otherwise.

(2) **WIRELESS TELECOMMUNICATIONS ~~UTILITY~~ SERVICE PROVIDER.** A provider of commercial mobile radio services as defined in the Code of Federal Regulations under 47 CFR 20.3. ~~A utility regulated by the Public Utilities Commission or the Common Carrier Bureau of the Federal Communications Commission which offers or provides wireless communication or paging services.~~

(3) **BUNDLED TRANSACTION.** The retail sale of a wireless telecommunications device which requires the retailer's customer to activate or contract with a wireless telecommunications utility service provider for utility service as a condition of that sale. A transaction is a bundled transaction within the meaning of this section without regard to the method in which the price is stated to the customer. Also, it is immaterial whether the wireless telecommunications device and utility service are sold for a single price or are separately itemized in the context of a sale or on a sales invoice.

(4) **UNBUNDLED SALES PRICE.** The price at which the a retailer would sell a specific wireless telecommunications device to a customer who is not required to activate or contract with a wireless telecommunications utility service provider for utility service as a condition of that sale. ~~The unbundled sales price of a wireless telecommunications device shall equal the fair retail selling price of that device and shall be consistent with the industry's usual or customary retail pricing practices for the type of device sold.~~

~~(5) **CARRIER RESTRICTED TRANSACTION.** The sale of a wireless telecommunications device which requires the customer purchasing the device to contract with one specific wireless telecommunications utility service provider for utility service as a condition of that sale. The customer purchasing the wireless telecommunications device is generally required to pay a predetermined fee to the wireless telecommunications utility service provider in the event that customer fails to obtain utility service from that wireless telecommunications utility service provider. The person providing the wireless telecommunications device to the customer does not receive a rebate or payment for obtaining the customer's contract with that wireless telecommunications utility service provider.~~

(6) **RETAIL UTILITIES TRANSACTION.** The combined retail sale of a wireless telecommunications device and utility service by a single retailer not affiliated with, or part of, a wireless telecommunications utility service provider. The retailer of a wireless telecommunications device purchases utility service from a wireless telecommunications utility service provider for sale directly to its customer. Customers are required to contract for utility service from the retailer upon the sale of a wireless telecommunications device to that customer. The sales price listed on the customer's sales receipt or invoice for the wireless telecommunications device may or may not be below the retailer's acquisition cost of that device. The customer continues to pay the retailer for utility service throughout the duration of the utility service contract.

Regulation 1585.  
CELLULAR TELEPHONES, PAGERS, AND OTHER  
WIRELESS TELECOMMUNICATION DEVICES.

(b) APPLICATION OF TAX.

(1) IN GENERAL. Tax applies to the gross receipts from the retail sale of a wireless telecommunications device. The retailer of the wireless telecommunications device is required to report and pay the tax.

(2) BUNDLED TRANSACTIONS AND RETAIL ~~UTILITIES~~ TRANSACTIONS. Tax applies to the gross receipts from the retail sale of a wireless telecommunication device sold in a bundled transaction or in a retail ~~utilities~~ transaction, measured by the unbundled sales price of that device. Tax applies to the unbundled sales price whether the wireless telecommunications device and utility service are sold for a single price or are separately itemized in the context of a sale or on a sales invoice. The retailer of the wireless telecommunications device is required to report and pay tax measured by the unbundled sales price of the device and may collect tax or tax reimbursement from its customer measured by the unbundled sales price. Tax does not apply to the charges in excess of the unbundled sales price made for telecommunications services.

(3) ~~CONSIGNMENT CARRIER RESTRICTED~~ TRANSACTIONS. Where the wireless telecommunications ~~utility~~ service provider retains title to the wireless communications device and consigns the wireless communications device to a third party for sale or lease to customers, that wireless telecommunications service provider is generally regarded as the retailer of the wireless telecommunications device notwithstanding any agreement of contractual obligation between the wireless telecommunications ~~utility~~ service provider and the person or entity providing the device to an end-use customer. Where the wireless telecommunications ~~utility~~ service provider provides consideration ~~reimburses or rebates money~~ to a separate person or entity, that person or entity receiving the consideration ~~reimbursement or rebate~~ is regarded as the retailer of the wireless telecommunication device. In either event, the person or entity regarded as the retailer of the wireless telecommunications device owes tax to the Board measured by the unbundled sales price of that device. If the retailer is the wireless telecommunications service provider, the wireless telecommunications service provider may reduce (or take a credit for) the amount of California sales tax due using the unbundled price approach by the amount of sales tax paid by the consumer on the retail transaction. ~~The retailer may not collect tax or tax reimbursement from either the end use customer or the person selling the device to the end use customer.~~

(4) ~~ACTIVATION FEES.~~ Tax does not apply to a one time charge for activating a new wireless telecommunication device with, or on behalf of, a utility service provider where the charge is separately stated and is not for the electronic or physical modification of the device in order for it to function within a utility service provider's service network. ~~A one time charge for activating a wireless telecommunication device is subject to tax if the activation consists of the physical or electronic modification or fabrication of a wireless telecommunication device in order for the device to function within a utility service provider's service network. The person collecting this fee is required to report and pay tax on that amount. Any subsequent charge for the physical or electronic modification or fabrication of that device which changes the customer's telephone number or which allows that customer to utilize a different utility service provider is subject to tax as set forth in Regulation 1546 (18 CCR 1546).~~

Regulation 1585.  
CELLULAR TELEPHONES, PAGERS, AND OTHER  
WIRELESS TELECOMMUNICATION DEVICES.

(c) **BAD DEBT DEDUCTIONS.**

(1) **IN GENERAL.** The provision of Regulation 1642, "Bad Debts" (18 CCR 1642) apply to retailers making sales of wireless telecommunications devices pursuant to subdivision (b)(1).

(2) **CHARGE-BACKS TO THE RETAILER.** Retailers reporting tax measured by the unbundled sales price of a wireless telecommunications device may take a bad debt deduction pursuant to Regulation 1642 when ~~consideration a payment or rebate~~ from a utility service provider is charged-back to the retailer based on a customer's termination of its contract with the utility service provider before the date specified in the utility service contract. The amount of bad debt deduction claimed by a retailer may not exceed the difference between the gross receipts on which tax was reported and paid by the retailer, and the total amount collected and retained by retailer from the sale of the wireless telecommunication device excluding any amounts collected from the customer as tax or tax reimbursement. Any tax or tax reimbursement collected by the retailer on the amount of bad debt deduction claimed by the retailer constitutes excess tax reimbursement and must be returned to the customer or paid to the Board unless the customer and retailer agree that this amount may be applied toward the amounts owed by the customer on the debt. The customer and retailer will be regarded as having agreed to the application of any excess tax reimbursement to the customer's debt where the retailer's books reflect both the debt owed by the customer and the corresponding credit for excess tax reimbursement.

(3) **RETAIL UTILITY TRANSACTIONS.** Retailers of wireless telecommunication devices sold in a retail utilities transaction may take a bad debt deduction pursuant to Regulation 1642 when a customer terminates its utility service contract with the retailer before the date specified in the utility service contract. The amount of bad debt deduction claimed by a retailer may not exceed the difference between the gross receipts on which tax was reported and paid by the retailer, and the total amount collected and retained by the retailer in connection with the sale of the wireless telecommunication device excluding any amounts collected from the customers as tax or tax reimbursement. The amount collected from the customer on the retail utility transaction shall be allocated among the total amount collected for both the wireless telecommunication device and utility service by dividing the unbundled sales price by the total amount the retailer would have collected if the customer fully performed under the terms of the utility service contract, and then multiplying that amount by the total amount collected by the retailer to date.

Any tax or tax reimbursement collected by the retailer on the amount of bad debt deduction claimed by the retailer constitutes excess tax reimbursement and must be returned to the customer or paid to the Board unless the customer and retailer agree that this amount may be applied toward the amounts owed by the customer on the bad debt. The customer and retailer will be regarded as having agreed to the application of any excess tax reimbursement to the customer's debt where the retailer's books reflect both the bad debt owed by the customer and the corresponding credit for excess tax reimbursement.

NOTE: Authority cited: Section 7051, Revenue and Taxation Code.

Reference:

Sections 6006, 6010, 6011, 6012, and 6055, Revenue and  
Taxation Code.

## REGULATION 1585 COMPARISON

PAGE 1

### Regulation 1585 - Cellular Telephones, Pagers, and Other Telecommunications Devices *Comparison Between Staff's Version and Industry's Suggested Changes*

STAFF'S PROPOSED LANGUAGE	INDUSTRY'S PROPOSED CHANGES	COMMENTS
(a) DEFINITIONS.	(a) DEFINITIONS.	
(1) WIRELESS TELECOMMUNICATION DEVICE. A portable communication device such as a cellular telephone or pager requiring activation by a utility service provider or seller of utility services in order to send, receive, or send and receive transmissions via network of wireless transmitters throughout multiple service areas, or otherwise.	(1) WIRELESS TELECOMMUNICATION DEVICE. A portable communication device such as a cellular telephone or pager requiring activation by a <u>wireless telecommunications</u> <del>utility</del> -service provider or seller of utility services in order to send, receive, or send and receive transmissions via network of wireless transmitters throughout multiple service areas, or otherwise.	Staff agrees to the proposed change.
(2) UTILITY SERVICE PROVIDER. A utility regulated by the Public Utilities Commission or the Common Carrier Bureau of the Federal Communications Commission which offers or provides wireless communication or paging services.	(2) <u>WIRELESS TELECOMMUNICATIONS</u> <del>UTILITY</del> SERVICE PROVIDER. <u>A provider of commercial mobile radio services as defined in the Code of Federal Regulations under 47 CFR 20.3.</u> <del>A utility regulated by the Public Utilities Commission or the Common Carrier Bureau of the Federal Communications Commission which offers or provides wireless communication or paging services.</del>	Staff disagrees with this proposal for the following reasons: 1) Proposed Regulation 1585 would be subject to definitional changes that may occur as a result of modifications to the CFR. For example, if 47 CFR 20.3 was modified by Congress or the FCC, the regulation would also be changed; and, 2) 47 CFR 20.3 does not appear to cover all aspects of wireless telecommunications as contemplated by proposed Regulation 1585.
(3) BUNDLED TRANSACTION. The retail sale of a wireless telecommunication device which requires the retailer's customer to contract with a utility service provider for utility service as a condition of that sale. A transaction is a bundled transaction within the meaning of this section without regard to the method in which the price is stated to the customer. Also, it is immaterial whether the wireless telecommunication device and utility service are sold for a single price or are separately itemized in the context of a sale or on a sales invoice.	(3) BUNDLED TRANSACTION. The retail sale of a wireless telecommunication device which requires the retailer's customer to <u>activate or</u> contract with a <u>wireless telecommunications</u> <del>utility</del> -service provider for utility service as a condition of that sale. A transaction is a bundled transaction within the meaning of this section without regard to the method in which the price is stated to the customer. Also, it is immaterial whether the wireless telecommunication device and utility service are sold for a single price or are separately itemized in the context of a sale or on a sales invoice.	Staff agrees to the proposed change.

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(4) UNBUNDLED SALES PRICE. The price at which a retailer would sell a specific wireless telecommunication device to a customer who is not required to activate or contract with a utility service provider for utility service as a condition of that sale. The unbundled sales price of a wireless telecommunication device shall equal the fair retail selling price of that device and shall be consistent with the industry's usual and customary retail pricing practices for the type of device sold.

(4) UNBUNDLED SALES PRICE. The price at which ~~the~~ a retailer would sell a specific wireless telecommunication device to a customer who is not required to activate or contract with a wireless telecommunications utility service provider for utility service as a condition of that sale. ~~The unbundled sales price of a wireless telecommunication device shall equal the fair retail selling price of that device and shall be consistent with the industry's usual and customary retail pricing practices for the type of device sold.~~

Staff believes this language should be left in, but that it could be modified to reflect the pricing practices of local retailers. Staff and industry do agree that the regulation should address the sale of discontinued and obsolete merchandise. Staff believes that industry "lined-out" language should be replaced with: "the unbundled sales price of a wireless telecommunications device shall equal the fair retail selling price of that device and shall be consistent with the usual and customary retail pricing practices of other local retailers for the type of device sold. The unbundled sales price of an obsolete wireless telecommunications device shall equal the actual selling price of that device." Staff also recommends that the words "would sell" on line one be changed to "has sold."

(5) CARRIER RESTRICTED TRANSACTION. The sale of a wireless telecommunication device which requires the customer purchasing the device to contract with one specific utility service provider for utility service as a condition of that sale. The customer purchasing the wireless telecommunication device is generally required to pay a predetermined fee to the utility service provider in the event that customer fails to obtain utility service from that utility service provider. The person providing the wireless telecommunication device to the customer does not receive a rebate or payment for obtaining the customer's contract with that utility service provider.

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Industry proposes that the name for these types of transactions be changed to "Consignment Transactions" and that language defining these transactions be copied from a portion of industry's proposed revisions to subdivision (b)(3). Staff disagrees. These types of transactions are not always consignment sales in that the person transferring the device to the end-use customer often has title to the device. Industry's proposed definition also fails to recognize that the end-use customer is required to contract exclusively with a particular service provider as a condition of purchasing the wireless device. Staff does believe that the term "Carrier Restricted Transaction" should be replaced with the term "Exclusive Service Provider Transactions" for clarification purposes.

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(6) RETAIL UTILITIES TRANSACTION. The combined retail sale of a wireless telecommunication device and utility service by a single retailer not affiliated with, or a part of, a utility service provider. The retailer of a wireless telecommunication device purchases utility service from a utility service provider for sale directly to its customer. Customers are required to contract for utility service from the retailer upon the sale of a wireless telecommunication device to that customer. The sales price listed on the customer's sales receipt or invoice for the wireless telecommunication device may or may not be below the retailer's acquisition cost of that device. The customer continues to pay the retailer for utility service throughout the duration of the utility service contract.

(b) APPLICATION OF TAX.

(1) IN GENERAL. Tax applies to the gross receipts from the retail sale of a wireless telecommunication device. The retailer of the wireless telecommunication device is required to report and pay the tax.

(2) BUNDLED TRANSACTIONS AND RETAIL UTILITIES TRANSACTIONS. Tax applies to the gross receipts from the retail sale of a wireless telecommunication device sold in a bundled transaction or in a retail utilities transaction, measured by the unbundled sales price of that device. Tax applies to the unbundled sales price whether the wireless telecommunication device and utility service are sold for a single price or are separately itemized in the context of a sale or on a sales invoice. The retailer of the wireless telecommunication device is required to report and pay tax measured by the unbundled sales

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Industry proposes a different name for the definition of this type of transaction. Staff remains of the opinion that the word "utilities" is necessary for describing these types of transactions.

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price of the device and may collect tax or tax reimbursement from its customer measured by the unbundled sales price. Tax does not apply to the charges in excess of the unbundled sales price made for telecommunication services

(3) CARRIER RESTRICTED TRANSACTIONS. The utility service provider is generally regarded as the retailer of the wireless telecommunication device notwithstanding any agreement or contractual obligation between the utility service provider and the person or entity providing the device to an end-use customer. Where the utility service provider reimburses or rebates money to a separate person or entity, that person or entity receiving the reimbursement or rebate is regarded as the retailer of the wireless telecommunication device. In either event, the person or entity regarded as the retailer of the wireless telecommunication device owes tax to the Board measured by the unbundled sales price of that device. The retailer may not collect tax or tax reimbursement from either the end-use customer or the person selling the device to the end-use customer.

(4) ACTIVATION FEES. Tax does not apply to a one-time charge for activating a new

price of the device and may collect tax or tax reimbursement from its customer measured by the unbundled sales price. Tax does not apply to the charges in excess of the unbundled sales price made for telecommunication services

(3) CONSIGNMENT CARRIER RESTRICTED TRANSACTIONS. Where the wireless telecommunications utility service provider retains title to the wireless communications device and consigns the wireless communications device to a third party for sale or lease to customers, that wireless telecommunications service provider is generally regarded as the retailer of the wireless telecommunication device notwithstanding any agreement or contractual obligation between the wireless telecommunications utility service provider and the person or entity providing the device to an end-use customer. Where the wireless telecommunications utility service provider provides consideration reimburses or rebates money to a separate person or entity, that person or entity receiving the consideration reimbursement or rebate is regarded as the retailer of the wireless telecommunication device. In either event, the person or entity regarded as the retailer of the wireless telecommunication device owes tax to the Board measured by the unbundled sales price of that device. If the retailer is the wireless telecommunications service provider, the wireless telecommunications service provider may reduce (or take credit for) the amount of California sales tax due using the unbundled price approach by the amount of sales tax paid by the consumer on the retail transaction. The retailer may not collect tax or tax reimbursement from either the end-use customer or the person selling the device to the end-use customer.

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Industry continues to classify all transactions as consignment sales and proposes that two separate entities pay tax measured by a portion of the total amount collected from an end-use customer. (This would also mean that two separate entities would attempt to collect tax reimbursement from a single, end-use customer.) Staff disagrees with this proposal. As set forth in staff's response to subdivision (a)(5), not all transactions within this category are consignment sales. Staff further believes that allowing two different entities to report tax on a portion of the total amount collected from an end-use customer would create consumer protection problems as well as administrative difficulties in performing audits. One alternative is to allow the person deemed the retailer for the transaction to report tax measured by the entire unbundled sales price of the wireless telecommunications device.

Staff believes that industry no longer objects to the provisions of this subdivision. However, one other

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wireless telecommunication device with, or on behalf of, a utility service provider where the charge is separately stated and is not for the electronic or physical modification of the device in order for it to function within a utility service provider's service network. A one-time charge for activating a wireless telecommunication device is subject to tax if the activation consists of the physical or electronic modification or fabrication of a wireless telecommunication device in order for the device to function within a utility service provider's service network. The person collecting this fee is required to report and pay tax on that amount. Any subsequent charge for the physical or electronic modification or fabrication of that device which changes the customer's telephone number or which allows that customer to utilize a different utility service provider is subject to tax as set forth in Regulation 1546 (18 CCR 1546).

### (c) BAD DEBT DEDUCTIONS.

(1) IN GENERAL. The provisions of Regulation 1642, "Bad Debts" (18 CCR 1642), apply to retailers making sales of wireless telecommunication devices pursuant to subdivision (b)(1).

(2) CHARGE-BACKS TO THE RETAILER. Retailers reporting tax measured by the unbundled sales price of a wireless telecommunication device may take a bad debt deduction pursuant to Regulation 1642 when a payment or rebate from a utility service provider is charged-back to the retailer based on a customer's termination of its contract with the utility service provider before the date specified in the utility service contract. The amount of bad debt deduction claimed by a retailer may not exceed the difference between the gross receipts on which tax was reported and paid by the retailer, and the total amount collected

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interested party has suggested that language be added to clarify what constitutes electronic modification.

Industry proposes that the words "a payment or rebate" be substituted with the word "consideration." Staff disagrees with this proposal. The word consideration is a technical legal term, with a particular meaning and consequences. The regulation uses terms commonly understood in the business community, in accordance with rulemaking requirements.

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and retained by the retailer from the sale of the wireless telecommunication device excluding any amounts collected from the customer as tax or tax reimbursement. Any tax or tax reimbursement collected by the retailer on the amount of bad debt deduction claimed by the retailer constitutes excess tax reimbursement and must be returned to the customer or paid to the Board unless the customer and retailer agree that this amount may be applied toward the amounts owed by the customer on the debt. The customer and retailer will be regarded as having agreed to the application of any excess tax reimbursement to the customer's debt where the retailer's books reflect both the debt owed by the customer and the corresponding credit for excess tax reimbursement.

### (3) RETAIL UTILITY TRANSACTIONS.

Retailers of wireless telecommunication devices sold in a retail utilities transaction may take a bad debt deduction pursuant to Regulation 1642 when a customer terminates its utility service contract with the retailer before the date specified in the utility service contract. The amount of bad debt deduction claimed by a retailer may not exceed the difference between the gross receipts on which tax was reported and paid by the retailer, and the total amount collected and retained by the retailer in connection with the sale of the wireless telecommunication device excluding any amounts collected from the customer as tax or tax reimbursement. The amount collected from the customer on the retail utility transaction shall be allocated among the total amount collected for both the wireless telecommunication device and utility service by dividing the unbundled sales price by the total amount the retailer would have collected if the customer fully performed under the terms of the utility service contract, and then multiplying that amount by the total amount collected by the retailer to date.

Any tax or tax reimbursement collected by the retailer

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