

Regulation 1525.2 & 1525.3

Section 100

Complete Rule Making File

OAL Approval with Approved Text Regulation 1525.2 &1523.3

Index

1. *Form 400 and Proposed Regulation 1525.2 &1523.3*
2. *Statement of Explanation*
3. **SB 38**

Other Documents Relied upon

- A. *Chief Counsel Memo Dated 04/03/14*
- B. *Draft Minutes, 04/22/14*
- C. *Reporters Transcript, 04/22/14*

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Enclosures

State of California
Office of Administrative Law

RECEIVED

JUN 06 2014

In re:

Board of Equalization

Regulatory Action:

Title 18, California Code of Regulations

Adopt sections:

Amend sections:

Repeal sections: 1525.2, 1525.3

NOTICE OF APPROVAL OF CHANGES
WITHOUT REGULATORY EFFECT

by EXECUTIVE DIRECTOR'S OFFICE
OF THE BOARD OF EQUALIZATION

California Code of Regulations, Title 1,
Section 100

OAL File No. 2014-0523-04 N

This action without regulatory effect repeals the partial exemption from sales and use tax for certain property used in specified activities, including manufacturing, pursuant to the expiration of statutory authority.

OAL approves this change without regulatory effect as meeting the requirements of California Code of Regulations, Title 1, section 100.

Date: 6/5/2014



Kathleen Eddy
Senior Attorney

For: DEBRA M. CORNEZ
Director

Original: Cynthia Bridges
Copy: Richard Bennion

NOTICE PUBLICATION/REGULATIONS SUBMISSION

(See instructions on reverse)

For use by Secretary of State only

STD. 400 (REV. 01-2013)

OAL FILE NUMBERS	NOTICE FILE NUMBER	REGULATORY ACTION NUMBER	EMERGENCY NUMBER
	Z-	2014-0523-04N	

ENDORSED FILED
 2014 JUN -5 PM 1:51

For use by Office of Administrative Law (OAL) only

2014 MAY 23 PM 2:24
 OFFICE OF ADMINISTRATIVE LAW

NOTICE	REGULATIONS
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Debra Bowen
 DEBRA BOWEN
 SECRETARY OF STATE

AGENCY WITH RULEMAKING AUTHORITY
 State Board of Equalization

AGENCY FILE NUMBER (if any)

A. PUBLICATION OF NOTICE (Complete for publication in Notice Register)

1. SUBJECT OF NOTICE	TITLE(S)	FIRST SECTION AFFECTED	2. REQUESTED PUBLICATION DATE
3. NOTICE TYPE <input type="checkbox"/> Notice re Proposed Regulatory Action <input type="checkbox"/> Other	4. AGENCY CONTACT PERSON	TELEPHONE NUMBER	FAX NUMBER (Optional)
OAL USE ONLY <input type="checkbox"/> Approved as Submitted <input type="checkbox"/> Approved as Modified <input type="checkbox"/> Disapproved/Withdrawn	ACTION ON PROPOSED NOTICE	NOTICE REGISTER NUMBER	PUBLICATION DATE

B. SUBMISSION OF REGULATIONS (Complete when submitting regulations)

1a. SUBJECT OF REGULATION(S) Manufacturing Equipment	1b. ALL PREVIOUS RELATED OAL REGULATORY ACTION NUMBER(S)
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2. SPECIFY CALIFORNIA CODE OF REGULATIONS TITLE(S) AND SECTION(S) (Including title 26, if toxics related)

SECTION(S) AFFECTED (List all section number(s) individually. Attach additional sheet if needed.)	ADOPT
	AMEND
	REPEAL
TITLE(S) 18	1525.2, 1525.3

3. TYPE OF FILING

<input type="checkbox"/> Regular Rulemaking (Gov. Code §11346)	<input type="checkbox"/> Certificate of Compliance: The agency officer named below certifies that this agency complied with the provisions of Gov. Code §§11346.2-11347.3 either before the emergency regulation was adopted or within the time period required by statute.	<input type="checkbox"/> Emergency Readopt (Gov. Code, §11346.1(h))	<input checked="" type="checkbox"/> Changes Without Regulatory Effect (Cal. Code Regs., title 1, §100)
<input type="checkbox"/> Resubmittal of disapproved or withdrawn nonemergency filing (Gov. Code §§11349.3, 11349.4)	<input type="checkbox"/> Resubmittal of disapproved or withdrawn emergency filing (Gov. Code, §11346.1)	<input type="checkbox"/> File & Print	<input type="checkbox"/> Print Only
<input type="checkbox"/> Emergency (Gov. Code, §11346.1(b))		<input type="checkbox"/> Other (Specify)	

4. ALL BEGINNING AND ENDING DATES OF AVAILABILITY OF MODIFIED REGULATIONS AND/OR MATERIAL ADDED TO THE RULEMAKING FILE (Cal. Code Regs. title 1, §44 and Gov. Code §11347.1)

5. EFFECTIVE DATE OF CHANGES (Gov. Code, §§ 11343.4, 11346.1(d); Cal. Code Regs., title 1, §100)

<input type="checkbox"/> Effective January 1, April 1, July 1, or October 1 (Gov. Code §11343.4(a))	<input type="checkbox"/> Effective on filing with Secretary of State	<input checked="" type="checkbox"/> §100 Changes Without Regulatory Effect	<input type="checkbox"/> Effective other (Specify)
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6. CHECK IF THESE REGULATIONS REQUIRE NOTICE TO, OR REVIEW, CONSULTATION, APPROVAL OR CONCURRENCE BY, ANOTHER AGENCY OR ENTITY

<input type="checkbox"/> Department of Finance (Form STD. 399) (SAM §6660)	<input type="checkbox"/> Fair Political Practices Commission	<input type="checkbox"/> State Fire Marshal
<input type="checkbox"/> Other (Specify)		

7. CONTACT PERSON Richard E. Bennion	TELEPHONE NUMBER (916) 445-2130	FAX NUMBER (Optional) (916) 324-3984	E-MAIL ADDRESS (Optional) rbennion@boe.ca.gov
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8. I certify that the attached copy of the regulation(s) is a true and correct copy of the regulation(s) identified on this form, that the information specified on this form is true and correct, and that I am the head of the agency taking this action, or a designee of the head of the agency, and am authorized to make this certification.

SIGNATURE OF AGENCY HEAD OR DESIGNEE <i>Joann Richmond</i>	DATE May 23, 2014
TYPED NAME AND TITLE OF SIGNATORY Joann Richmond, Chief, Board Proceedings Division	

For use by Office of Administrative Law (OAL) only

ENDORSED APPROVED

JUN 05 2014

Office of Administrative Law

Text of Proposed Changes to

Title 18. Public Revenue

1525.2. Manufacturing Equipment.

(a) ~~Partial Exemption for Property Purchased for Use in the Manufacturing Process. Section 6377 of the Revenue and Taxation Code provides a partial exemption from sales and use tax for certain properties described in this regulation.~~

~~For the period commencing on January 1, 1994, and ending on December 31, 1994, the partial exemption applies to the taxes imposed by the state (6%), but does not apply to the taxes imposed by counties, cities, and districts pursuant to the Bradley Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code § 7200, et seq.) or the Transactions and Use Tax Law (Rev. & Tax. Code §§ 7251, et seq.).~~

~~For the period commencing on January 1, 1995, and ending on December 31, 2000, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2001, and ending on December 31, 2001, the partial exemption applies to the taxes imposed by sections 6051 and 6201 of the Revenue and Taxation Code (4.75%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2002, and ending on December 31, 2003, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~Pursuant to the provisions of the Revenue and Taxation Code section 6377(g), the partial exemption from tax on the sale and use of property used in manufacturing and related activities as described in this regulation expired on December 31, 2003.~~

~~Subject to the limitations set forth above, this partial exemption applies to gross receipts from the sale, storage, use, or other consumption in this state of the following items:~~

- ~~(1) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point that raw materials are received by the qualified person and introduced into the process and ending at the point at which the property has been altered to its completed form, including packaging, if required. For purposes of this regulation:~~

~~(A) Raw materials will be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified person's manufacturing activities are conducted. Raw materials that are stored on premises other than where the qualified person's manufacturing activities are conducted, however, will not be considered to have been introduced into the process for purposes of this regulation.~~

~~(B) For purposes of this regulation, the term "packaging" includes only that packaging necessary to prepare the goods for delivery to and placement in the qualified person's finished goods inventory, or to prepare the goods so that they are suitable for delivery to and placement in finished goods inventory. Any additional packaging, such as that packaging necessary to consolidate the goods prior to shipping or to protect them during transportation, shall not be considered to be "packaging" for purposes of this regulation.~~

~~(2) Tangible personal property purchased for use by a qualified person to be used primarily in research and development as defined in subdivision (c)(8).~~

~~(3) Tangible personal property purchased for use by a qualified person to be used primarily to maintain, repair, measure, or test any property described in subdivision (a)(1) or (a)(2).~~

~~(4) Tangible personal property purchased for use by a contractor purchasing that property either as an agent of a qualified person or for the contractor's own account and subsequent resale to a qualified person for use in the performance of a construction contract for the qualified person who will use the tangible personal property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, or as a research or storage facility for use in connection with the manufacturing process.~~

~~(b) Property Used Primarily in Administration, General Management, or Marketing.~~

~~Notwithstanding any other provision of this regulation, this partial exemption shall not apply to any tangible personal property that is used primarily in administration, general management, or marketing. For purposes of this subdivision:~~

~~(1) Tangible personal property is used primarily in administration, general management, or marketing when it is used 50 percent or more of the time in one or more of those activities.~~

~~(2) Tangible personal property used primarily to clean and maintain the factory floor of a manufacturing facility is used primarily in a stage of the manufacturing of property and is not used primarily in administration, general management, or marketing.~~

~~(3) Fire safety equipment that is tangible personal property and that is used primarily at and in connection with the factory floor of a manufacturing facility is used primarily in a stage of the manufacturing of property and is not used primarily in administration, general management, or marketing.~~

~~(c) Definitions. For purposes of this regulation:~~

(1) “Fabricating” means to make, build, create, produce, or assemble components or property to work in a new or different manner.

(2) “Manufacturing” means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or for use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property. For purposes of this regulation, “greater functionality” means that the tangible personal property has been improved so that it can perform new or different functions than the original property. Manufacturing includes logging, that is, the felling of timber, but does not include tree farming. Manufacturing does not include crop harvesting. Provided that the activity constitutes a “sale” as that term is used in subdivision (b) of section 6006 of the Revenue and Taxation Code, the tangible personal property need not be owned by the qualified person in order for the activity to qualify as manufacturing for purposes of this regulation.

(3) “Primarily” means that the tangible personal property is used 50 percent or more of the time in the designated activity or activities.

(4) “Process” means the period beginning at the point at which any raw materials are received by the qualified person and are introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified person and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified person has altered tangible personal property to its completed form including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified person's manufacturing, processing, refining, or recycling activity is conducted. Raw materials that are stored on premises other than where the qualified person's manufacturing, processing, refining, fabricating, or recycling activity is conducted, shall not be considered to have been introduced into the manufacturing, processing, refining, fabricating, or recycling process.

(5) “Processing” means the physical application of materials and labor to modify or change the characteristics of property.

(6) “Qualified person” means any person that satisfies the requirements of both subdivisions (e)(6)(A) and (e)(6)(B) below with regard to the trade or business in which the property will be placed into service in the use qualifying the property for this partial exemption:

(A) A “qualified person” must have first commenced trade or business activities in a new trade or business in this state on or after January 1, 1994. For purposes of this subdivision, the term “activities” means trade or business activities. In determining whether or not a person is qualified within the meaning of this subdivision, the following rules apply:

1. The term “trade or business activities” does not mean the mere formation or organization of a corporation or other business entity that is intended to conduct a trade or business. Instead, a corporation or business entity first conducts activities when it first starts or commences the trade or business for which it was organized. The acquisition of operating assets that are necessary to the type of business contemplated, however, will constitute commencing activities. The term “operating assets” as used in this subdivision means assets that are in a state of readiness to be placed in service within a reasonable time period following their acquisition.

2. Notwithstanding any other provision of this subdivision, a person will not be considered to have first commenced activities in a new trade or business in this state on or after January 1, 1994, if, at any time within the 36 months preceding that date, that person, or any related person, was required to have secured a seller's permit under section 6066 of the Revenue and Taxation Code for that trade or business, or any other trade or business classified under the same division of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition (the “Manual”). For purposes of this regulation, the term “division” means a division as that term is used in the Manual.

3. A trade or business is not a new trade or business in this state if, within the 36 months preceding the date that activities were first commenced in that trade or business in this state, either the person claiming the partial exemption, or any related person, had conducted any activities in this state in any trade or business classified under the same division of the Manual as that trade or business.

4. Where a person, or any related person, is engaged in one or more trade or business activities in this state, or has been engaged in one or more trade or business activities in this state within the preceding 36 months (a “prior trade or business activity”), and thereafter commences an additional trade or business activity in this state, the additional trade or business activity shall only be treated as a new trade or business if the additional trade or business activity is classified under a different division of the Manual than are any of the person's (or any related person's) current or prior trade or business activities in this state within the preceding 36 months.

5. Where a person, including all related persons, is engaged in trade or business activities wholly outside of this state and that person first commences doing business in this state (within the meaning of section 23101 of the Revenue and Taxation Code) after December 31, 1993 (other than by purchase or other acquisition described in subdivision (c)(6)(A)6., the newly commenced trade or business activity in this state shall be treated as a new trade or business for purposes of this subdivision.

6. On or after January 1, 1995, notwithstanding anything else set forth in this subdivision, in any case where a person purchases or otherwise acquires all or any portion of the assets of an existing trade or business (irrespective of the form of the entity) that is doing business in this state (within the meaning of section 23101 of the

Revenue and Taxation Code), the trade or business thereafter conducted by that person (or any related person) shall not be treated as a new trade or business if the aggregate fair market value of the acquired assets (including real, personal, tangible, and intangible property) used by that person (or any related person) in the conduct of his or her trade or business exceeds 20 percent of the aggregate fair market value of the total assets of the person (or any related person) being used in the same trade or business both within and without this state. For purposes of this subdivision only:

a. The determination of the relative fair market values of the acquired assets and the total assets shall be made as of the last day of the month following the quarterly period in which the person (or any related person) first uses any of the acquired trade or business assets in his or her business activity.

b. Any acquired assets that constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the transferor shall not be treated as assets acquired from an existing trade or business, unless those assets also constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the acquiring person (or any related person).

c. The trade or business conducted in this state by the acquiring person after the asset acquisition date shall be considered to be the same as an out-of-state trade or business conducted or previously conducted by the acquiring person (or any related person) only if the trade or business activities of both companies are or would be classified in the same division of the Manual.

d. An acquired trade or business will not be considered to have been acquired as an existing trade or business for purposes of this subdivision if it is acquired either: (1) from a liquidation sale of assets pursuant to a bankruptcy filed under Chapter 7 of the United States Bankruptcy Code; or (2) pursuant to a creditor's execution or foreclosure sale of a secured interest in the assets of the trade or business.

e. Example No. 1: Corporation X is doing business wholly outside of this state in the trade or business of manufacturing automobiles. The total fair market value of the total assets of this trade or business is \$100,000,000. Then, on or after January 1, 1994, Corporation X acquires all of the assets of an automobile manufacturing business in this state with a fair market value of \$5,000,000 and immediately uses the acquired assets in its automobile manufacturing trade or business. Thereafter, between the date of acquisition and the last day of the month following the quarterly period during which the acquisition occurred, Corporation X acquires another \$1,000,000 in assets for use in the automobile manufacturing business in this state. Under these assumed facts, the conditions set forth in this subparagraph will not serve to disqualify Corporation X from the partial exemption since the fair market value of the acquired assets does not exceed 20 percent ($\$5,000,000/\$106,000,000$) of the aggregate fair market value of the total assets of

~~the trade or business being conducted by Corporation X; and neither Corporation X nor any related person had conducted any trade or business activities in this state within the preceding 36 months.~~

~~f. Example No. 2: Assume the same facts as in Example No. 1 above, but in this case, prior to acquiring the assets of the automobile manufacturing business in this state, Corporation X was solely and exclusively in the trade or business of providing data processing services. After the acquisition of the assets by Corporation X, however, the acquired assets will continue to be used in the automobile manufacturing business in this state. Assume further that no additional purchases are made after the date of acquisition. Under these assumed facts, since data processing services and automobile manufacturing are classified in different divisions of the Manual, the partial exemption will not be available to Corporation X because the fair market value of the acquired assets exceeds 20 percent (\$5,000,000/\$5,000,000) of the aggregate fair market value of the total assets held by Corporation X in the same trade or business.~~

~~7. In any case where the legal form under which a trade or business activity is being conducted is changed, the change in form shall be disregarded and the determination of whether the trade or business activity is a new business shall be made by treating the person as having purchased or otherwise acquired all or any portion of the assets of an existing trade or business. For purposes of this subdivision only:~~

~~a. Example No. 1: Corporation X is doing business in this state. One of its trade or business activities in this state is manufacturing automobiles. After January 1, 1994, for consideration, Corporation X transfers all of the assets used in the trade or business of manufacturing automobiles to a newly formed, wholly owned subsidiary known as Corporation Y. For purposes of applying this regulation, this transaction shall be treated as an acquisition of an existing trade or business by Corporation Y.~~

~~b. Example No. 2: Partnership A is a manufacturer doing business in this state. After January 1, 1994, for consideration, Partnership A transfers all of its assets to a newly formed corporation known as Corporation B. Corporation B is owned by the partners of Partnership A in the same proportionate ownership interests as their respective ownership interests in the partnership. For purposes of applying this regulation, this transaction shall be treated as an acquisition of an existing trade or business by Corporation B.~~

~~8. For purposes of this subdivision, a person is a "related person" if that person is or previously was related to the qualified person within the meaning of either section 267 or 318 of the Internal Revenue Code.~~

~~9. The term "acquire" shall include any gift, inheritance, transfer incident to divorce, or any other transfer, whether or not for consideration.~~

~~(B) A qualified person must be engaged in those manufacturing lines of business described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition. For purposes of this subdivision:~~

~~1. For purposes of classifying a line or lines of business, the economic unit shall be the "establishment" and the classification of the line or lines of business will be based on the establishment's single most predominant activity based upon value of production. The term "establishment" means an economic unit, generally at a single physical location, where business is conducted or where services or manufacturing or other industrial operations are performed. The following will generally constitute an "establishment": a factory, mill, store, hotel, movie theater, mine, farm, ranch, bank, railroad depot, airline terminal, sales office, warehouse, or central administrative office.~~

~~2. For purposes of determining the "establishment" or "establishments" of a trade or business:~~

~~a. Where distinct and separate economic activities are performed at a single physical location, such as construction activities operated out of the same physical location as a lumber yard, each activity should be treated as a separate establishment where: (i) no one industry description in the classification includes such combined activities; (ii) the employment in each such economic activity is significant; and (iii) separate reports are prepared on the number of employees, their wages and salaries, sales or receipts, property and equipment, and other types of financial data, such as financial statements, job costing, and profit center accounting. For purposes of this paragraph, whether or not employment in an economic activity is significant shall be based upon all of the facts and circumstances. Nevertheless, employment in an economic activity will be considered to be "significant" for purposes of this paragraph whenever more than 25 percent of the taxpayer's total number of employees at a single physical location, or more than 25 percent of the taxpayer's total dollar value of payroll at a single physical location, is attributable to the economic activity being tested for separate establishment status.~~

~~b. An establishment is not necessarily identical with the enterprise or company which may consist of one or more establishments. Also, an establishment is to be distinguished from subunits of the establishment such as departments.~~

~~c. Where a person conducts business at more than one establishment within the meaning of this subdivision, then that person shall be considered to be a "qualified person" for purposes of this regulation only as to those purchases that are intended to be used and are actually used in those lines of business that are described in Codes 2011 to 3999, inclusive, of the Standard Industrial~~

Classification Manual published by the United States Office of Management and Budget, 1987 edition.

(7) “Refining” means the process of converting a natural resource to an intermediate or finished product.

(8) “Research and development” means those activities that are described in section 174 of the Internal Revenue Code or in any regulations thereunder.

(9) “Tangible personal property” does not include any of the following:

(A) Real property, including tangible personal property to be incorporated into an improvement to real property, except for “special purpose buildings and foundations” as defined in subdivision (c)(10)(D) and conveyance systems and assembly lines as provided in subdivision (c)(10)(A).

(B) Consumables with a normal useful life of less than one year, except as provided in subdivision (c)(10)(E). For purposes of this regulation, it shall be presumed tangible personal property that the qualified person treats as having a normal useful life of less than one year for state income or franchise tax purposes is tangible personal property with a normal useful life of less than one year. This presumption may be rebutted by evidence satisfactory to the Board.

(C) Furniture, inventory, equipment used in the extraction process, equipment used to store raw materials that have not yet entered or commenced the manufacturing process, or equipment used to store finished products that have completed the manufacturing process. The extraction process includes such severance activities as mining, oil and gas extraction.

(D) Any property for which a credit is claimed under either section 17053.49 or 23649 of the Revenue and Taxation Code.

(10) “Tangible personal property” includes but is not limited to the following:

(A) Machinery and equipment within the meaning of subdivision (a)(6) of Regulation 1521 of the Sales and Use Tax Regulations, including component parts and contrivances such as belts, shafts, moving parts, and operating structures. The term also includes conveyance systems and assembly lines without regard to the manner of affixation to real property.

(B) All equipment or devices used or required to operate, control, regulate, or maintain the machinery, including, without limitation, computers, data processing equipment, and computer software, including both operating programs and application programs, together with all repair and replacement parts with a useful life of one or more years therefor, whether purchased separately or in conjunction with a complete machine and

~~regardless of whether the machine or component parts are assembled by the taxpayer or another party. Any repair and replacement parts that the qualified person treats as having a useful life of less than one year for state income or franchise tax purposes shall be presumed to have a useful life of less than one year for purposes of this regulation. This presumption may be rebutted by evidence satisfactory to the Board.~~

~~(C) Property used in pollution control that meets or exceeds standards established by this state or any local or regional governmental agency within this state.~~

~~(D) Special purpose buildings and foundations that (i) are used as an integral part of the manufacturing, processing, refining, or fabricating process, or (ii) constitute a research facility used during the manufacturing process as an integral part of a manufacturing, processing, refining, or fabricating activity, or (iii) constitute a storage facility used during the manufacturing process as an integral part of a manufacturing, processing, refining, or fabricating activity. For purposes of this subdivision:~~

~~1. For purposes of this subdivision, "special purpose building and foundation" means only a building and the foundation immediately underlying the building that is specifically designed and constructed or reconstructed for the installation, operation, and use of specific machinery and equipment with a special purpose, which machinery and equipment, after installation, will become affixed to or a fixture of the real property, and the construction or reconstruction of which is specifically designed and used exclusively for the specified purposes as set forth in subdivision (a)(1) of this regulation (the qualified purpose).~~

~~2. A building is specifically designed and constructed or modified for a qualified purpose if it is not economic to design and construct the building for the intended purpose and then use the structure for a different purpose.~~

~~3. A building is used exclusively for a qualified purpose only if its use does not include a use for which it was not specifically designed and constructed or modified. Incidental use of a building for non-qualified purposes does not preclude the building from being a special purpose building. "Incidental use" means a use which is both related and subordinate to the qualified purpose. A use is not subordinate if more than one-third of the total usable volume of the building is devoted to a use which is not a qualifying purpose.~~

~~4. In the event an entire building does not qualify as a special purpose building, a taxpayer may establish that a portion of a building, and the foundation immediately underlying the portion, qualifies for treatment as a special purpose building and foundation if the portion satisfies all of the definitional provisions in this subdivision.~~

~~5. Buildings and foundations that do not meet the definition of a special purpose building and foundation set forth above include, but are not limited to, buildings designed and constructed or reconstructed principally to function as a general purpose~~

~~manufacturing, industrial, or commercial building; research facilities that are used primarily prior to or after, or prior to and after, the manufacturing process; or storage facilities that are used primarily prior to or after, or prior to and after, completion of the manufacturing process.~~

~~6. For purposes of this subdivision, the term "integral part" means that the special purpose building or foundation (i) is used directly in the activity qualifying for the partial exemption from sales and use tax and (ii) is essential to the completeness of that activity. In determining whether property is used as an integral part of manufacturing, all properties used by the qualified person in processing the raw materials into the final product are properties used as an integral part of manufacturing.~~

~~(E) Fuels used or consumed in the manufacturing process.~~

~~(F) Property used in recycling.~~

~~(11) "Standard Industrial Classification" means a Standard Industrial Classification in the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition.~~

~~(d) Three Year Limitation. Notwithstanding any other provision of this regulation, once a person has conducted business activities in a new trade or business for three or more years, that person will no longer be considered to be in a "new trade or business," nor "qualified" for this partial exemption.~~

~~(e) Taxes as to Which the Partial Exemption Does Not Apply. This partial exemption does not apply to any tax levied by a county, city, or district pursuant to, or in accordance with, either the Bradley Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code §§7200 et seq.) or the Transactions and Use Tax Law (Rev. & Tax Code §§7251 et seq.).~~

~~On or after January 1, 1995, this partial exemption shall not apply to any tax levied pursuant to section 6051.2 and 6201.2 of the Revenue and Taxation Code, or pursuant to section 35 of article XIII of the California Constitution.~~

~~(f) Exemption Certificates. Except as otherwise set forth in subdivision (f)(3), to claim the partial exemption provided by this regulation, a person must be both pre-qualified by the Board and either registered to hold a seller's permit or maintain a consumer use tax account. Exemption certificates issued to qualified persons will contain a control number and expiration date for verifying a person's status as a qualified person. An exemption certificate is not valid if it has not been issued by the Board or if it is accepted after the expiration date on the certificate. Qualified persons who have been pre-qualified may reproduce the issued certificates as needed for their qualifying purchases.~~

The exemption certificates issued by the Board will be in substantially the same form as they appear in Appendices A and B of this regulation. Qualified persons who purchase or lease tangible personal property from an in-state retailer or an out-of-state retailer obligated to collect the use tax must provide the retailer with a manufacturer's exemption certificate in order to claim the partial exemption. The manufacturer's use tax declaration must be completed by a qualified person to claim a partial exemption from use tax on purchases of tangible personal property from an out-of-state retailer not obligated to collect the use tax.

Solely for the purposes of this regulation, it is presumed that a seller accepts a manufacturer's exemption certificate from a prequalified purchaser in good faith in the absence of evidence to the contrary. A retailer's direct knowledge that the purchaser is not purchasing tangible personal property for use in a manufacturing activity, that the purchaser intends the tangible personal property for his or her own use, or that the tangible personal property does not have a normal useful life of one year or more constitutes evidence to the contrary. A purchaser providing a manufacturer's exemption certificate accepted in good faith by the seller for tangible personal property that does not qualify for this exemption is liable for the payment of tax as set forth in subdivision (h).

(1) ~~Manufacturer's Exemption Certificates.~~

(A) ~~In General. Except as otherwise provided in subdivisions (f)(1)(B) or (f)(3) of this regulation, or in section 6902.2 of the Revenue and Taxation Code, a partial exemption from sales or use tax shall not be allowed unless:~~

- ~~1. The qualified person furnishes the retailer with a manufacturer's exemption certificate no later than 60 days after the date of the purchase; and~~
- ~~2. The retailer timely files a sales and use tax return claiming the partial exemption and, together with that timely return, provides the Board with a copy of the manufacturer's exemption certificate.~~

(B) ~~Exclusions. Except as provided in subdivision (f)(1)(C) below, retailers claiming the partial exemption in timely filed returns will not be required to furnish the Board with copies of manufacturer's exemption certificates for sales or leases of tangible personal property made by a retailer at any single physical location to a single qualified purchaser that do not exceed an aggregate total of \$25,000 during a single calendar quarter. Regardless of the total quarterly sales per purchaser, however, when necessary for the efficient administration of the sales and use tax law, the Board may, on 30 days' written notice, require a retailer to commence furnishing the Board with copies of all certificates on a quarterly basis pursuant to subdivision (f)(1)(A)2.~~

(C) ~~Retention and Availability of Certificates. A retailer must retain each manufacturer's exemption certificate received from a qualified person for a period of four years from the date on which the retailer claims a partial exemption based on the exemption certificate.~~

~~Within 45 days of the Board's request, retailers must furnish to the Board any and all manufacturer's exemption certificates, or copies thereof, received from qualified persons, including exemption certificates for aggregate sales or leases of \$25,000 or less to a single qualified person made at any single physical location of the retailer during a single calendar quarter.~~

~~(2) Manufacturer's Use Tax Declaration. Except as provided in section 6902.2 of the Revenue and Taxation Code, a partial exemption from the use tax shall not be allowed unless the qualified person:~~

~~(A) Timely files a sales and use tax return or consumer use tax return for the period in which the purchase occurs and timely pays any applicable tax in full that is excluded from this partial exemption as provided in subdivision (e) of this regulation; and~~

~~(B) Attaches a completed manufacturer's use tax declaration to the sales and use tax return or consumer use tax return that is timely filed with the Board.~~

~~(3) Refund of Partial Exemption.~~

~~(A) For the period commencing on January 1, 1994, and ending on December 31, 1994, a qualified person may claim the partial exemption on qualified purchases from an in-state retailer or an out-of-state retailer obligated to collect the use tax by furnishing the retailer with a manufacturer's exemption certificate on or before March 31, 1995. The retailer must refund the tax directly to the purchaser or, at the purchaser's sole option, the purchaser may be credited with such amount. In the event that the retailer has already reported and paid the tax to the Board, the retailer must file a written claim for refund on or before April 30, 1995.~~

~~(B) A person who paid sales tax on a qualified sale or paid use tax on a qualified purchase and who failed to claim the partial exemption as provided by this regulation may file a claim for refund equal to the amount of the partial exemption that he or she could have claimed pursuant to this regulation. The procedure for such a claim shall be the same as for other claims for refund filed pursuant to Revenue and Taxation Code section 6901. For transactions subject to use tax, a person filing a claim for refund of the partial exemption has the burden of establishing that he or she was entitled to claim the partial exemption with respect to the amount of refund claimed under this part. For transactions subject to sales tax, a person filing a claim for refund of the partial exemption has the burden of establishing that the purchaser of the qualified property otherwise met all the requirements of a qualified person at the time of the purchase subject to the refund claimed under this part.~~

~~(4) Construction Contractors. In the case of a contractor who purchases property as an agent of a qualified person or for subsequent resale to a qualified person, the qualified person is deemed to be the purchaser for purposes of this subdivision.~~

~~(g) Conversion of Property to a Use Not Qualifying for the Partial Exemption. Notwithstanding subdivision (a), this partial exemption shall not apply to any sale of, or the storage, use, or other consumption in this state of property that, within one year from the later of the date of purchase of the property or the date that the property was first placed into service by the purchaser in an exempt use, is: (i) removed from this state, (ii) converted from an exempt use under this regulation to some other use not qualifying for the partial exemption, or (iii) used in a manner not qualifying for the partial exemption under this regulation. For purposes of this subdivision, property is converted to a use not qualifying for the partial exemption if, without limitation, the property, or any interest in the property, or possession or control of the property, is either directly or indirectly sold, transferred, leased, or assigned to a person who is not a qualified person on the date the property is sold, transferred, leased, or assigned to such non-qualified person. In the case of a corporation that, as a qualified person, purchases tangible personal property under this partial exemption and then, within one year from the later of the date of purchase of the property or the date that the property was first placed into service by that corporation in an exempt use, either directly or indirectly transfers that property to its parent corporation that is not a qualified person on the date of the transfer of property to the parent corporation, that property has been converted to a use not qualifying for the partial exemption.~~

~~(h) Purchaser's Liability for the Payment of Sales Tax. If a purchaser submits a copy of a manufacturer's exemption certificate to the seller, and then within one year from the later of the date of purchase of the property or the date that the property was first placed into service by the purchaser in an exempt use, the purchaser either (i) removes that property from this state, (ii) converts that property from an exempt use under this regulation to some other use not qualifying for the partial exemption, or (iii) uses that property in a manner not qualifying for the partial exemption under this regulation, then, in that event, the purchaser shall be liable for payment of sales tax, with applicable interest, to the same extent as if the purchaser were a retailer making a retail sale of the property at the time the property was so removed, converted, or used; and the sales price of the property to the purchaser shall be deemed to be the gross receipts from that retail sale. For purposes of this subdivision, property is converted to a use not qualifying for the partial exemption if, without limitation, the property, or any interest in the property, or possession or control of the property, is either directly or indirectly sold, transferred, leased, or assigned to a person who is not a qualified person on the date the property is sold, transferred, leased, or assigned to such nonqualified person.~~

~~(i) Leases to Qualifying Persons:~~

~~(1) Leases—In General. Subject to all the limitations and conditions set forth in this regulation and regulation 1525.3, this partial exemption may apply to rental receipts paid by a qualified person with respect to a lease of tangible personal property to the qualified person, which tangible personal property is used as set forth in subdivisions (a)(1), (a)(2), (a)(3), or (a)(4) of this regulation.~~

~~(2) Leases—Acquisition Sale and Leaseback. A person will be regarded as having paid sales tax reimbursement or use tax with respect to that person's purchase of property, within the meaning of those words as they are used in section 6010.65 of the Revenue and Taxation~~

~~Code, if the person has paid all applicable taxes with respect to the acquisition of the property, notwithstanding the fact that the sale and purchase of the property may have been subject to the partial exemption from tax provided by this regulation.~~

~~(3) Subsequent Lease of Property Acquired Subject to Partial Exemption. If a person has acquired property subject to the partial exemption provided by this regulation and has paid all applicable taxes at that acquisition, the property will be regarded as property as to which sales tax reimbursement or use tax has been paid, and the subsequent lease of that property will not be subject to tax measured by rental receipts.~~

~~(j) Operative Date. Except as expressly set forth otherwise in subdivisions (e)(6)(A)6. and (e) of this regulation, this regulation is operative as of January 1, 1994. All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or a use made after December 31, 2003.~~

~~Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Section 6377, Revenue and Taxation Code.~~

Appendix A

SECTION 6377 MANUFACTURER'S EXEMPTION CERTIFICATE

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

PLEASE NOTE

This exemption being declared applies only to the state use tax which is at the rate of 6% effective January 1, 2002, 4.75% from January 1, 2001 to December 31, 2001, and 5% from January 1, 1995 to December 31, 2000, and is specific to this transaction only and may not be construed to exempt other transactions. As the purchaser, you remain liable for the applicable local and district taxes. To claim the exemption, this declaration must accompany a timely filed sales and use tax return for the period of purchase. Void after expiration date. Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or a use made after December 31, 2003. Questions regarding this certificate should be directed to: [insert contact information]

<p>Certificate No:</p> <p>Valid Period Begins:</p> <p>Valid Period Expires:</p> <p>(*See below for leases)</p>

I hereby certify that the tangible personal property described below and purchased or leased from:
(enter seller's/lessor's name and address)

SELLER'S NAME

SELLER'S ADDRESS (Street, City, State, Zip Code)

and will be used by me primarily (please check one)

- 1. for manufacturing, processing, refining, fabricating, or recycling, or
- 2. for research and development activities as described in Internal Revenue Code Section 174, or
- 3. to maintain, repair, measure, or test any property being used for (1) or (2) above, at my facility located

at (enter facility's address):

(Street, City, State, Zip Code)

SALES INVOICE NUMBER	SALES INVOICE DATE	DESCRIPTION OF QUALIFIED PROPERTY PURCHASED OR LEASED*	SALES PRICE/ RENTALS PAYABLE

I understand that if such property is, within one year from the date of purchase or lease, removed from California or converted for use or otherwise used in a manner not qualifying for the partial exemption that I am required by the Sales and Use Tax Law to report and pay the state tax measured by the sales price/rentals payable of the property to/by me. Taxable rentals payable from the lease of certain tangible personal property to a qualified person are subject to the partial exemption for a period of six years from the date of inception of the lease. The lease must commence during the time in which this Certificate is valid. *Attach a copy of the lease agreement.

PRINT NAME OF PURCHASER OR PURCHASER'S AUTHORIZED REPRESENTATIVE	TITLE	
SIGNATURE	DATE	PERMIT NUMBER

****NOT VALID UNLESS COMPLETED BY THE CALIFORNIA STATE BOARD OF EQUALIZATION**

The following business has been registered as a "qualified person" who has certified that this purchase/lease of tangible personal property will be used in a manner entitling them to the exemption provided in Section 6377 of the Revenue and Taxation Code.

BUSINESS NAME	SIC CODE
BUSINESS ADDRESS (Street, City, State, Zip Code)	PERMIT NUMBER

****AUTHORIZED BY: (Must be signed by two Board representatives)**

REVIEWED BY	DATE
APPROVED BY	DATE

**** WHEN COMPLETED AND SIGNED, THIS FORM MAY BE REPRODUCED FOR USE BY THE QUALIFIED PERSON LISTED ABOVE**

Appendix B

SECTION 6377 MANUFACTURER'S USE TAX DECLARATION

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

PLEASE NOTE

This is a partial exemption from sales and use taxes at the rate of 5% effective January 1, 2002, 4.75% from January 1, 2001 to December 31, 2001, and 5% from January 1, 1995 to December 31, 2000. You are not relieved from your obligations for the local and district taxes on this transaction. The exemption is specific to this transaction only and may not be construed to exempt other transactions. Generally, the partial exemption will not be allowed unless this certificate is issued within 60 days after the date of purchase and the retailer claims the exemption on a timely filed return. Void after expiration date. Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for sales made after December 31, 2003. Questions regarding this certificate should be directed to: [insert contact information]

Certificate No:
Valid Period Begins:
Valid Period Expires:
(*See below for leases)

I hereby certify that the tangible personal property described below that is subject to use tax was purchased or is being leased from: (enter seller's/lessor's name and address)

SELLER'S NAME

SELLER'S ADDRESS (Street, City, State, Zip Code)

and will be used by me primarily (please check one)

- 1. for manufacturing, processing, refining, fabricating, or recycling, or
- 2. for research and development activities as described in Internal Revenue Code Section 174, or
- 3. to maintain, repair, measure, or test any property being used for (1) or (2) above, at my facility located at (enter facility's address):

(Street, City, State, Zip Code)

SALES INVOICE NUMBER	SALES INVOICE DATE	DESCRIPTION OF PROPERTY PURCHASED OR LEASED*	SALES PRICE/ RENTALS PAYABLE

I understand that if such property is, within one year from the date of purchase or lease, removed from California or converted for use or otherwise used in a manner not qualifying for the partial exemption that I am required by the Sales and Use Tax Law to report and pay the state tax measured by the sales price/rentals payable of the property to/by me. Taxable rentals payable from the lease of certain tangible personal property to a qualified person are subject to the partial exemption for a period of six years from the date of inception of the lease. The lease must commence during the time in which this Certificate is valid. *Attach a copy of the lease agreement.

PRINT NAME OF PURCHASER OR PURCHASER'S AUTHORIZED REPRESENTATIVE	TITLE	
SIGNATURE	DATE	PERMIT NUMBER

**** NOT VALID UNLESS COMPLETED BY THE CALIFORNIA STATE BOARD OF EQUALIZATION**

The following business has been registered as a "qualified person" who has certified that this purchase/lease of tangible personal property will be used in a manner entitling them to the exemption provided in Section 6377 of the Revenue and Taxation Code.

BUSINESS NAME	SIC CODE
BUSINESS ADDRESS (Street, City, State, Zip Code)	PERMIT NUMBER

****AUTHORIZED BY: (Must be signed by two Board representatives)**

REVIEWED BY	DATE
APPROVED BY	DATE

**** WHEN COMPLETED AND SIGNED, THIS FORM MAY BE REPRODUCED FOR USE BY THE QUALIFIED PERSON LISTED ABOVE**

Text of Proposed Changes to

Title 18. Public Revenue

~~1525.3. Manufacturing Equipment—Leases of Tangible Personal Property.~~

~~(a) General Application to Leases. Leases of tangible personal property which are classified as “continuing sales” and “continuing purchases” of tangible personal property, in accordance with Regulation 1660, “Leases of Tangible Personal Property—In General,” may qualify for the partial exemption from tax for manufacturing equipment, under the conditions set forth in paragraph (i)(1) of Regulation 1525.2, “Manufacturing Equipment.” Lease transactions which qualify for the partial exemption are taxed at the rate specified in Regulation 1525.2, paragraph (a).~~

~~(b) Recharacterization. With respect to transactions which the parties denominate as a “lease,” but which are recharacterized for sales and use tax purposes either as sales at their inception, pursuant to Regulation 1641, “Credit Sales and Repossessions,” paragraph (b), or as sales under a security agreement, Regulation 1660, “Leases of Tangible Personal Property—In General,” paragraph (a)(2), the transactions may qualify for the partial exemption, in accordance with Regulation 1525.2.~~

~~(c) Continuation of Partial Exemption. Where possession of tangible personal property is transferred to a qualified person as defined in paragraphs (c) and (d) of Regulation 1525.2 and pursuant to a lease agreement classified as a continuing sale and continuing purchase, lease receipts shall remain partially exempt for a period of six years from the date of the inception of the lease whether or not the lessee remains as a qualified person throughout the six year period. At the close of the six year period from the date of the inception of the lease, lease receipts are subject to tax without exemption.~~

~~(d) Leases of Tax Paid Property. The partial exemption is not available to lessors who lease to qualified persons or to vendors to such lessors when the lessor elects to pay sales tax reimbursement at the time of acquisition of the property or pays use tax measured by the purchase price of the property.~~

~~(e) Manufacturers Who Lease Qualified Property. A lease of tangible personal property by the manufacturer of that property is ordinarily regarded as a “continuing sale” and “continuing purchase” in accordance with Regulation 1660, “Leases of Tangible Personal Property—In General.” Nevertheless, beginning January 1, 1997, a lessor of tangible personal property described in sections 17053.49 or 23649 of the Revenue and Taxation Code, who is the manufacturer of that property and who leases that property to a qualified person, as defined in section 17053.49 or 23649 of the Revenue and Taxation Code, in a form that is not substantially the same form as acquired, may, in lieu of reporting tax measured by the rentals payable, elect to pay tax measured by the cost price of that property where the election is made on or before the due date of the return for the period in which the property is first leased to the qualified person. The election shall be made by reporting use tax measured by the cost price of that property on the return for that period. The election shall not be revoked with respect to the property as to which it is made. The lease of that property for which an election is made to report and pay tax on the cost price of that property shall thereafter be excluded from the classification of a “continuing sale” and “continuing purchase.”~~

For purposes of this subdivision, "cost price" means the price at which similar property has been previously sold or offered for sale. If that property has not been previously sold or offered for sale, then the cost price shall be deemed to be the aggregate of the following:

(1) Cost of materials.

(2) Direct labor.

(3) The pro rata share of all overhead costs attributable to the manufacturer of the property.

(4) Reasonable profit from the manufacturing operations which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the factors listed in subsections (1) to (3), inclusive.

~~(f) Operative Date. All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or use made after December 31, 2003.~~

~~Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6244.5 and 6377, Revenue and Taxation Code.~~

SUMMARY OF REGULATORY ACTIONS

REGULATIONS FILED WITH SECRETARY OF STATE

This Summary of Regulatory Actions lists regulations filed with the Secretary of State on the dates indicated. Copies of the regulations may be obtained by contacting the agency or from the Secretary of State, Archives, 1020 O Street, Sacramento, CA 95814, (916) 653-7715. Please have the agency name and the date filed (see below) when making a request.

File# 2014-0509-02
 BOARD OF EQUALIZATION
 Returns, Defects and Replacements

This rulemaking action by the State Board of Equalization (Board) amends Section 1655, Title 18, of the California Code of Regulations. These amendments align section 1655 with Civil Code sections 1793.2 and 1793.25, as amended by Statutes 2011, Chapter 727 (AB 242), relating to reimbursement of sales and use taxes previously paid to the Board by a motor vehicle manufacturer when the manufacturer subsequently pays restitution to a consumer pursuant to Civil Code section 1793.2.

Title 18
 California Code of Regulations
 AMEND: 1655
 Filed 06/11/2014
 Effective 10/01/2014
 Agency Contact:
 Richard E. Bennion (916) 445-2130

File# 2014-0523-04
 BOARD OF EQUALIZATION
 Manufacturing Equipment

This action without regulatory effect repeals the partial exemption from sales and use tax for certain property used in specified activities, including manufacturing, pursuant to the expiration of statutory authority.

Title 18
 California Code of Regulations
 REPEAL: 1525.2, 1525.3
 Filed 06/05/2014
 Agency Contact:
 Richard E. Bennion (916) 445-2130

File# 2014-0429-02
 BOARD OF FORESTRY AND FIRE PROTECTION
 Road Rules, 2013

This regulatory action by the Board of Forestry and Fire Protection (Board) represents a comprehensive overhaul of the Board's "Road Rules," located within title 14 of the California Code of Regulations. The purpose of this action is to ensure that all road-related Forest Practice Rules adequately prevent individual and cumulative adverse impacts to beneficial uses of water. In addition to making substantive revisions, the Board reorganized all rules related to logging roads, landings, and watercourse crossings into a clear, concise, and logical order.

Title 14
 California Code of Regulations
 ADOPT: 923, 923.1, 923.2, 923.3, 923.4, 923.5, 923.6, 923.7, 923.8, 923.9, 923.9.1, 943, 943.1, 943.2, 943.3, 943.4, 943.5, 943.6, 943.7, 943.8, 943.9, 943.9.1, 963, 963.1, 963.2, 963.3, 963.4, 963.5, 963.6, 963.7, 963.8, 963.9, 963.9.1 AMEND: 895.1, 914.7, 914.8, 915.1, 916.3, 916.4, 916.9, 934.7, 934.8, 935.1, 936.3, 936.4, 936.9, 954.7, 954.8, 955.1, 956.3, 956.4, 956.9, 1034, 1051.1, 1090.5, 1090.7, 1092.09, 1093.2, 1104.1 REPEAL: 918.3, 923, 923.1, 923.2, 923.3, 923.4, 923.5, 923.6, 923.7, 923.8, 923.9, 923.9.1, 938.3, 943, 943.1, 943.2, 943.3, 943.4, 943.5, 943.6, 943.7, 943.8, 943.9, 943.9.1, 958.3, 963, 963.1, 963.2, 963.3, 963.4, 963.5, 963.6, 963.7, 963.8, 963.9
 Filed 06/11/2014
 Effective 01/01/2015
 Agency Contact: George Gentry (916) 653-8031

File# 2014-0505-01
 CALIFORNIA GAMBLING CONTROL COMMISSION
 MICS IV-Cage Operations; Security of Floor Banks, Equipment, etc.

The California Gambling Control Commission amended two sections and adopted one section in title 4 of the California Code of Regulations pertaining to written policies and procedures containing minimum internal control standards (MICS) that California gambling establishments must maintain. The MICS are related to cage operation and functions, security of floor banks, and security of gambling equipment and confidential documents.

Regulation 1642

Section 100

Index

1. *Form 400 and Proposed Regulation 1525.2 &1523.3*
2. *Statement of Explanation*
3. **SB 38**

NOTICE PUBLICATION/REGULATIONS SUBMISSION

(See instructions on reverse)

For use by Secretary of State only

STD. 400 (REV. 01-2013)

OAL FILE NUMBERS	NOTICE FILE NUMBER Z-	REGULATORY ACTION NUMBER 2014-0523-04N	EMERGENCY NUMBER
For use by Office of Administrative Law (OAL) only			
NOTICE		REGULATIONS	
AGENCY WITH RULEMAKING AUTHORITY State Board of Equalization			AGENCY FILE NUMBER (If any)

2014 MAY 23 PM 2:21

OFFICE OF
ADMINISTRATIVE LAW**A. PUBLICATION OF NOTICE (Complete for publication in Notice Register)**

1. SUBJECT OF NOTICE	TITLE(S)	FIRST SECTION AFFECTED	2. REQUESTED PUBLICATION DATE
3. NOTICE TYPE <input type="checkbox"/> Notice re Proposed Regulatory Action <input type="checkbox"/> Other	4. AGENCY CONTACT PERSON	TELEPHONE NUMBER	FAX NUMBER (Optional)
OAL USE ONLY <input type="checkbox"/> Approved as Submitted <input type="checkbox"/> Approved as Modified <input type="checkbox"/> Disapproved/Withdrawn	ACTION ON PROPOSED NOTICE	NOTICE REGISTER NUMBER	PUBLICATION DATE

B. SUBMISSION OF REGULATIONS (Complete when submitting regulations)

1a. SUBJECT OF REGULATION(S) Manufacturing Equipment	1b. ALL PREVIOUS RELATED OAL REGULATORY ACTION NUMBER(S)
2. SPECIFY CALIFORNIA CODE OF REGULATIONS TITLE(S) AND SECTION(S) (Including title 26, if toxics related)	
SECTION(S) AFFECTED (List all section number(s) individually. Attach additional sheet if needed.)	ADOPT
	AMEND
TITLE(S) 18	REPEAL 1525.2, 1525.3
3. TYPE OF FILING	
<input type="checkbox"/> Regular Rulemaking (Gov. Code §11346)	<input type="checkbox"/> Certificate of Compliance: The agency officer named below certifies that this agency complied with the provisions of Gov. Code §§11346.2-11347.3 either before the emergency regulation was adopted or within the time period required by statute.
<input type="checkbox"/> Resubmittal of disapproved or withdrawn nonemergency filing (Gov. Code §§11349.3, 11349.4)	<input type="checkbox"/> Emergency Readopt (Gov. Code, §11346.1(h))
<input type="checkbox"/> Emergency (Gov. Code, §11346.1(b))	<input type="checkbox"/> Resubmittal of disapproved or withdrawn emergency filing (Gov. Code, §11346.1)
	<input type="checkbox"/> File & Print
	<input type="checkbox"/> Other (Specify) _____
	<input checked="" type="checkbox"/> Changes Without Regulatory Effect (Cal. Code Regs., title 1, §100)
	<input type="checkbox"/> Print Only
4. ALL BEGINNING AND ENDING DATES OF AVAILABILITY OF MODIFIED REGULATIONS AND/OR MATERIAL ADDED TO THE RULEMAKING FILE (Cal. Code Regs. title 1, §44 and Gov. Code §11347.1)	
5. EFFECTIVE DATE OF CHANGES (Gov. Code, §§ 11343.4, 11346.1(d); Cal. Code Regs., title 1, §100)	
<input type="checkbox"/> Effective January 1, April 1, July 1, or October 1 (Gov. Code §11343.4(a))	<input type="checkbox"/> Effective on filing with Secretary of State
	<input checked="" type="checkbox"/> \$100 Changes Without Regulatory Effect
	<input type="checkbox"/> Effective other (Specify) _____
6. CHECK IF THESE REGULATIONS REQUIRE NOTICE TO, OR REVIEW, CONSULTATION, APPROVAL OR CONCURRENCE BY, ANOTHER AGENCY OR ENTITY	
<input type="checkbox"/> Department of Finance (Form STD. 399) (SAM §6660)	<input type="checkbox"/> Fair Political Practices Commission
<input type="checkbox"/> Other (Specify) _____	<input type="checkbox"/> State Fire Marshal
7. CONTACT PERSON Richard E. Bennion	TELEPHONE NUMBER (916) 445-2130
	FAX NUMBER (Optional) (916) 324-3984
	E-MAIL ADDRESS (Optional) rbennion@boe.ca.gov

8. I certify that the attached copy of the regulation(s) is a true and correct copy of the regulation(s) identified on this form, that the information specified on this form is true and correct, and that I am the head of the agency taking this action, or a designee of the head of the agency, and am authorized to make this certification.

SIGNATURE OF AGENCY HEAD OR DESIGNEE <i>Joann Richmond</i>	DATE May 23, 2014
TYPED NAME AND TITLE OF SIGNATORY Joann Richmond, Chief, Board Proceedings Division	

For use by Office of Administrative Law (OAL) only

Text of Proposed Changes to

Title 18. Public Revenue

~~1525.2. Manufacturing Equipment.~~

~~(a) Partial Exemption for Property Purchased for Use in the Manufacturing Process. Section 6377 of the Revenue and Taxation Code provides a partial exemption from sales and use tax for certain properties described in this regulation.~~

~~For the period commencing on January 1, 1994, and ending on December 31, 1994, the partial exemption applies to the taxes imposed by the state (6%), but does not apply to the taxes imposed by counties, cities, and districts pursuant to the Bradley Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code § 7200, et seq.) or the Transactions and Use Tax Law (Rev. & Tax. Code §§ 7251, et seq.).~~

~~For the period commencing on January 1, 1995, and ending on December 31, 2000, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2001, and ending on December 31, 2001, the partial exemption applies to the taxes imposed by sections 6051 and 6201 of the Revenue and Taxation Code (4.75%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2002, and ending on December 31, 2003, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~Pursuant to the provisions of the Revenue and Taxation Code section 6377(g), the partial exemption from tax on the sale and use of property used in manufacturing and related activities as described in this regulation expired on December 31, 2003.~~

~~Subject to the limitations set forth above, this partial exemption applies to gross receipts from the sale, storage, use, or other consumption in this state of the following items:~~

- ~~(1) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point that raw materials are received by the qualified person and introduced into the process and ending at the point at which the property has been altered to its completed form, including packaging, if required. For purposes of this regulation:~~

(A) Raw materials will be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified person's manufacturing activities are conducted. Raw materials that are stored on premises other than where the qualified person's manufacturing activities are conducted, however, will not be considered to have been introduced into the process for purposes of this regulation.

(B) For purposes of this regulation, the term "packaging" includes only that packaging necessary to prepare the goods for delivery to and placement in the qualified person's finished goods inventory, or to prepare the goods so that they are suitable for delivery to and placement in finished goods inventory. Any additional packaging, such as that packaging necessary to consolidate the goods prior to shipping or to protect them during transportation, shall not be considered to be "packaging" for purposes of this regulation.

(2) Tangible personal property purchased for use by a qualified person to be used primarily in research and development as defined in subdivision (e)(8).

(3) Tangible personal property purchased for use by a qualified person to be used primarily to maintain, repair, measure, or test any property described in subdivision (a)(1) or (a)(2).

(4) Tangible personal property purchased for use by a contractor purchasing that property either as an agent of a qualified person or for the contractor's own account and subsequent resale to a qualified person for use in the performance of a construction contract for the qualified person who will use the tangible personal property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, or as a research or storage facility for use in connection with the manufacturing process.

(b) ~~Property Used Primarily in Administration, General Management, or Marketing.~~ Notwithstanding any other provision of this regulation, this partial exemption shall not apply to any tangible personal property that is used primarily in administration, general management, or marketing. For purposes of this subdivision:

(1) ~~Tangible personal property is used primarily in administration, general management, or marketing when it is used 50 percent or more of the time in one or more of those activities.~~

(2) ~~Tangible personal property used primarily to clean and maintain the factory floor of a manufacturing facility is used primarily in a stage of the manufacturing of property and is not used primarily in administration, general management, or marketing.~~

(3) ~~Fire safety equipment that is tangible personal property and that is used primarily at and in connection with the factory floor of a manufacturing facility is used primarily in a stage of the manufacturing of property and is not used primarily in administration, general management, or marketing.~~

(c) ~~Definitions.~~ For purposes of this regulation:

(1) "Fabricating" means to make, build, create, produce, or assemble components or property to work in a new or different manner.

(2) "Manufacturing" means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or for use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property. For purposes of this regulation, "greater functionality" means that the tangible personal property has been improved so that it can perform new or different functions than the original property. Manufacturing includes logging, that is, the felling of timber, but does not include tree farming. Manufacturing does not include crop harvesting. Provided that the activity constitutes a "sale" as that term is used in subdivision (b) of section 6006 of the Revenue and Taxation Code, the tangible personal property need not be owned by the qualified person in order for the activity to qualify as manufacturing for purposes of this regulation.

(3) "Primarily" means that the tangible personal property is used 50 percent or more of the time in the designated activity or activities.

(4) "Process" means the period beginning at the point at which any raw materials are received by the qualified person and are introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified person and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified person has altered tangible personal property to its completed form including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified person's manufacturing, processing, refining, or recycling activity is conducted. Raw materials that are stored on premises other than where the qualified person's manufacturing, processing, refining, fabricating, or recycling activity is conducted, shall not be considered to have been introduced into the manufacturing, processing, refining, fabricating, or recycling process.

(5) "Processing" means the physical application of materials and labor to modify or change the characteristics of property.

(6) "Qualified person" means any person that satisfies the requirements of both subdivisions (e)(6)(A) and (e)(6)(B) below with regard to the trade or business in which the property will be placed into service in the use qualifying the property for this partial exemption:

(A) A "qualified person" must have first commenced trade or business activities in a new trade or business in this state on or after January 1, 1994. For purposes of this subdivision, the term "activities" means trade or business activities. In determining whether or not a person is qualified within the meaning of this subdivision, the following rules apply:

1. The term “trade or business activities” does not mean the mere formation or organization of a corporation or other business entity that is intended to conduct a trade or business. Instead, a corporation or business entity first conducts activities when it first starts or commences the trade or business for which it was organized. The acquisition of operating assets that are necessary to the type of business contemplated, however, will constitute commencing activities. The term “operating assets” as used in this subdivision means assets that are in a state of readiness to be placed in service within a reasonable time period following their acquisition.

2. Notwithstanding any other provision of this subdivision, a person will not be considered to have first commenced activities in a new trade or business in this state on or after January 1, 1994, if, at any time within the 36 months preceding that date, that person, or any related person, was required to have secured a seller's permit under section 6066 of the Revenue and Taxation Code for that trade or business, or any other trade or business classified under the same division of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition (the “Manual”). For purposes of this regulation, the term “division” means a division as that term is used in the Manual.

3. A trade or business is not a new trade or business in this state if, within the 36 months preceding the date that activities were first commenced in that trade or business in this state, either the person claiming the partial exemption, or any related person, had conducted any activities in this state in any trade or business classified under the same division of the Manual as that trade or business.

4. Where a person, or any related person, is engaged in one or more trade or business activities in this state, or has been engaged in one or more trade or business activities in this state within the preceding 36 months (a “prior trade or business activity”), and thereafter commences an additional trade or business activity in this state, the additional trade or business activity shall only be treated as a new trade or business if the additional trade or business activity is classified under a different division of the Manual than are any of the person's (or any related person's) current or prior trade or business activities in this state within the preceding 36 months.

5. Where a person, including all related persons, is engaged in trade or business activities wholly outside of this state and that person first commences doing business in this state (within the meaning of section 23101 of the Revenue and Taxation Code) after December 31, 1993 (other than by purchase or other acquisition described in subdivision (c)(6)(A)6., the newly commenced trade or business activity in this state shall be treated as a new trade or business for purposes of this subdivision.

6. On or after January 1, 1995, notwithstanding anything else set forth in this subdivision, in any case where a person purchases or otherwise acquires all or any portion of the assets of an existing trade or business (irrespective of the form of the entity) that is doing business in this state (within the meaning of section 23101 of the

Revenue and Taxation Code), the trade or business thereafter conducted by that person (or any related person) shall not be treated as a new trade or business if the aggregate fair market value of the acquired assets (including real, personal, tangible, and intangible property) used by that person (or any related person) in the conduct of his or her trade or business exceeds 20 percent of the aggregate fair market value of the total assets of the person (or any related person) being used in the same trade or business both within and without this state. For purposes of this subdivision only:

a. The determination of the relative fair market values of the acquired assets and the total assets shall be made as of the last day of the month following the quarterly period in which the person (or any related person) first uses any of the acquired trade or business assets in his or her business activity.

b. Any acquired assets that constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the transferor shall not be treated as assets acquired from an existing trade or business, unless those assets also constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the acquiring person (or any related person).

c. The trade or business conducted in this state by the acquiring person after the asset acquisition date shall be considered to be the same as an out-of-state trade or business conducted or previously conducted by the acquiring person (or any related person) only if the trade or business activities of both companies are or would be classified in the same division of the Manual.

d. An acquired trade or business will not be considered to have been acquired as an existing trade or business for purposes of this subdivision if it is acquired either: (1) from a liquidation sale of assets pursuant to a bankruptcy filed under Chapter 7 of the United States Bankruptcy Code; or (2) pursuant to a creditor's execution or foreclosure sale of a secured interest in the assets of the trade or business.

e. Example No. 1: Corporation X is doing business wholly outside of this state in the trade or business of manufacturing automobiles. The total fair market value of the total assets of this trade or business is \$100,000,000. Then, on or after January 1, 1994, Corporation X acquires all of the assets of an automobile manufacturing business in this state with a fair market value of \$5,000,000 and immediately uses the acquired assets in its automobile manufacturing trade or business. Thereafter, between the date of acquisition and the last day of the month following the quarterly period during which the acquisition occurred, Corporation X acquires another \$1,000,000 in assets for use in the automobile manufacturing business in this state. Under these assumed facts, the conditions set forth in this subparagraph will not serve to disqualify Corporation X from the partial exemption since the fair market value of the acquired assets does not exceed 20 percent ($\$5,000,000/\$106,000,000$) of the aggregate fair market value of the total assets of

~~the trade or business being conducted by Corporation X; and neither Corporation X nor any related person had conducted any trade or business activities in this state within the preceding 36 months.~~

~~f. Example No. 2: Assume the same facts as in Example No. 1 above, but in this case, prior to acquiring the assets of the automobile manufacturing business in this state, Corporation X was solely and exclusively in the trade or business of providing data processing services. After the acquisition of the assets by Corporation X, however, the acquired assets will continue to be used in the automobile manufacturing business in this state. Assume further that no additional purchases are made after the date of acquisition. Under these assumed facts, since data processing services and automobile manufacturing are classified in different divisions of the Manual, the partial exemption will not be available to Corporation X because the fair market value of the acquired assets exceeds 20 percent ($\$5,000,000/\$5,000,000$) of the aggregate fair market value of the total assets held by Corporation X in the same trade or business.~~

~~7. In any case where the legal form under which a trade or business activity is being conducted is changed, the change in form shall be disregarded and the determination of whether the trade or business activity is a new business shall be made by treating the person as having purchased or otherwise acquired all or any portion of the assets of an existing trade or business. For purposes of this subdivision only:~~

~~a. Example No. 1: Corporation X is doing business in this state. One of its trade or business activities in this state is manufacturing automobiles. After January 1, 1994, for consideration, Corporation X transfers all of the assets used in the trade or business of manufacturing automobiles to a newly formed, wholly owned subsidiary known as Corporation Y. For purposes of applying this regulation, this transaction shall be treated as an acquisition of an existing trade or business by Corporation Y.~~

~~b. Example No. 2: Partnership A is a manufacturer doing business in this state. After January 1, 1994, for consideration, Partnership A transfers all of its assets to a newly formed corporation known as Corporation B. Corporation B is owned by the partners of Partnership A in the same proportionate ownership interests as their respective ownership interests in the partnership. For purposes of applying this regulation, this transaction shall be treated as an acquisition of an existing trade or business by Corporation B.~~

~~8. For purposes of this subdivision, a person is a "related person" if that person is or previously was related to the qualified person within the meaning of either section 267 or 318 of the Internal Revenue Code.~~

~~9. The term "acquire" shall include any gift, inheritance, transfer incident to divorce, or any other transfer, whether or not for consideration.~~

(B) A qualified person must be engaged in those manufacturing lines of business described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition. For purposes of this subdivision:

1. For purposes of classifying a line or lines of business, the economic unit shall be the "establishment" and the classification of the line or lines of business will be based on the establishment's single most predominant activity based upon value of production. The term "establishment" means an economic unit, generally at a single physical location, where business is conducted or where services or manufacturing or other industrial operations are performed. The following will generally constitute an "establishment": a factory, mill, store, hotel, movie theater, mine, farm, ranch, bank, railroad depot, airline terminal, sales office, warehouse, or central administrative office.

2. For purposes of determining the "establishment" or "establishments" of a trade or business:

a. Where distinct and separate economic activities are performed at a single physical location, such as construction activities operated out of the same physical location as a lumber yard, each activity should be treated as a separate establishment where: (i) no one industry description in the classification includes such combined activities; (ii) the employment in each such economic activity is significant; and (iii) separate reports are prepared on the number of employees, their wages and salaries, sales or receipts, property and equipment, and other types of financial data, such as financial statements, job costing, and profit center accounting. For purposes of this paragraph, whether or not employment in an economic activity is significant shall be based upon all of the facts and circumstances. Nevertheless, employment in an economic activity will be considered to be "significant" for purposes of this paragraph whenever more than 25 percent of the taxpayer's total number of employees at a single physical location, or more than 25 percent of the taxpayer's total dollar value of payroll at a single physical location, is attributable to the economic activity being tested for separate establishment status.

b. An establishment is not necessarily identical with the enterprise or company which may consist of one or more establishments. Also, an establishment is to be distinguished from subunits of the establishment such as departments.

c. Where a person conducts business at more than one establishment within the meaning of this subdivision, then that person shall be considered to be a "qualified person" for purposes of this regulation only as to those purchases that are intended to be used and are actually used in those lines of business that are described in Codes 2011 to 3999, inclusive, of the Standard Industrial

Classification Manual published by the United States Office of Management and Budget, 1987 edition.

(7) “Refining” means the process of converting a natural resource to an intermediate or finished product.

(8) “Research and development” means those activities that are described in section 174 of the Internal Revenue Code or in any regulations thereunder.

(9) “Tangible personal property” does not include any of the following:

(A) Real property, including tangible personal property to be incorporated into an improvement to real property, except for “special purpose buildings and foundations” as defined in subdivision (c)(10)(D) and conveyance systems and assembly lines as provided in subdivision (c)(10)(A).

(B) Consumables with a normal useful life of less than one year, except as provided in subdivision (c)(10)(E). For purposes of this regulation, it shall be presumed tangible personal property that the qualified person treats as having a normal useful life of less than one year for state income or franchise tax purposes is tangible personal property with a normal useful life of less than one year. This presumption may be rebutted by evidence satisfactory to the Board.

(C) Furniture, inventory, equipment used in the extraction process, equipment used to store raw materials that have not yet entered or commenced the manufacturing process, or equipment used to store finished products that have completed the manufacturing process. The extraction process includes such severance activities as mining, oil and gas extraction.

(D) Any property for which a credit is claimed under either section 17053.49 or 23649 of the Revenue and Taxation Code.

(10) “Tangible personal property” includes but is not limited to the following:

(A) Machinery and equipment within the meaning of subdivision (a)(6) of Regulation 1521 of the Sales and Use Tax Regulations, including component parts and contrivances such as belts, shafts, moving parts, and operating structures. The term also includes conveyance systems and assembly lines without regard to the manner of affixation to real property.

(B) All equipment or devices used or required to operate, control, regulate, or maintain the machinery, including, without limitation, computers, data processing equipment, and computer software, including both operating programs and application programs, together with all repair and replacement parts with a useful life of one or more years therefor, whether purchased separately or in conjunction with a complete machine and

regardless of whether the machine or component parts are assembled by the taxpayer or another party. Any repair and replacement parts that the qualified person treats as having a useful life of less than one year for state income or franchise tax purposes shall be presumed to have a useful life of less than one year for purposes of this regulation. This presumption may be rebutted by evidence satisfactory to the Board.

(C) Property used in pollution control that meets or exceeds standards established by this state or any local or regional governmental agency within this state.

(D) Special purpose buildings and foundations that (i) are used as an integral part of the manufacturing, processing, refining, or fabricating process, or (ii) constitute a research facility used during the manufacturing process as an integral part of a manufacturing, processing, refining, or fabricating activity, or (iii) constitute a storage facility used during the manufacturing process as an integral part of a manufacturing, processing, refining, or fabricating activity. For purposes of this subdivision:

1. For purposes of this subdivision, "special purpose building and foundation" means only a building and the foundation immediately underlying the building that is specifically designed and constructed or reconstructed for the installation, operation, and use of specific machinery and equipment with a special purpose, which machinery and equipment, after installation, will become affixed to or a fixture of the real property, and the construction or reconstruction of which is specifically designed and used exclusively for the specified purposes as set forth in subdivision (a)(1) of this regulation (the qualified purpose).

2. A building is specifically designed and constructed or modified for a qualified purpose if it is not economic to design and construct the building for the intended purpose and then use the structure for a different purpose.

3. A building is used exclusively for a qualified purpose only if its use does not include a use for which it was not specifically designed and constructed or modified. Incidental use of a building for non-qualified purposes does not preclude the building from being a special purpose building. "Incidental use" means a use which is both related and subordinate to the qualified purpose. A use is not subordinate if more than one-third of the total usable volume of the building is devoted to a use which is not a qualifying purpose.

4. In the event an entire building does not qualify as a special purpose building, a taxpayer may establish that a portion of a building, and the foundation immediately underlying the portion, qualifies for treatment as a special purpose building and foundation if the portion satisfies all of the definitional provisions in this subdivision.

5. Buildings and foundations that do not meet the definition of a special purpose building and foundation set forth above include, but are not limited to, buildings designed and constructed or reconstructed principally to function as a general purpose

manufacturing, industrial, or commercial building; research facilities that are used primarily prior to or after, or prior to and after, the manufacturing process; or storage facilities that are used primarily prior to or after, or prior to and after, completion of the manufacturing process.

6. For purposes of this subdivision, the term "integral part" means that the special purpose building or foundation (i) is used directly in the activity qualifying for the partial exemption from sales and use tax and (ii) is essential to the completeness of that activity. In determining whether property is used as an integral part of manufacturing, all properties used by the qualified person in processing the raw materials into the final product are properties used as an integral part of manufacturing.

(E) Fuels used or consumed in the manufacturing process.

(F) Property used in recycling.

(11) "Standard Industrial Classification" means a Standard Industrial Classification in the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition.

(d) Three Year Limitation. Notwithstanding any other provision of this regulation, once a person has conducted business activities in a new trade or business for three or more years, that person will no longer be considered to be in a "new trade or business," nor "qualified" for this partial exemption.

(e) Taxes as to Which the Partial Exemption Does Not Apply. This partial exemption does not apply to any tax levied by a county, city, or district pursuant to, or in accordance with, either the Bradley Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code §§7200 et seq.) or the Transactions and Use Tax Law (Rev. & Tax Code §§7251 et seq.).

On or after January 1, 1995, this partial exemption shall not apply to any tax levied pursuant to section 6051.2 and 6201.2 of the Revenue and Taxation Code, or pursuant to section 35 of article XIII of the California Constitution.

(f) Exemption Certificates. Except as otherwise set forth in subdivision (f)(3), to claim the partial exemption provided by this regulation, a person must be both pre-qualified by the Board and either registered to hold a seller's permit or maintain a consumer use tax account. Exemption certificates issued to qualified persons will contain a control number and expiration date for verifying a person's status as a qualified person. An exemption certificate is not valid if it has not been issued by the Board or if it is accepted after the expiration date on the certificate. Qualified persons who have been pre-qualified may reproduce the issued certificates as needed for their qualifying purchases.

~~The exemption certificates issued by the Board will be in substantially the same form as they appear in Appendices A and B of this regulation. Qualified persons who purchase or lease tangible personal property from an in-state retailer or an out-of-state retailer obligated to collect the use tax must provide the retailer with a manufacturer's exemption certificate in order to claim the partial exemption. The manufacturer's use tax declaration must be completed by a qualified person to claim a partial exemption from use tax on purchases of tangible personal property from an out-of-state retailer not obligated to collect the use tax.~~

~~Solely for the purposes of this regulation, it is presumed that a seller accepts a manufacturer's exemption certificate from a prequalified purchaser in good faith in the absence of evidence to the contrary. A retailer's direct knowledge that the purchaser is not purchasing tangible personal property for use in a manufacturing activity, that the purchaser intends the tangible personal property for his or her own use, or that the tangible personal property does not have a normal useful life of one year or more constitutes evidence to the contrary. A purchaser providing a manufacturer's exemption certificate accepted in good faith by the seller for tangible personal property that does not qualify for this exemption is liable for the payment of tax as set forth in subdivision (h).~~

~~(1) Manufacturer's Exemption Certificates.~~

~~(A) In General. Except as otherwise provided in subdivisions (f)(1)(B) or (f)(3) of this regulation, or in section 6902.2 of the Revenue and Taxation Code, a partial exemption from sales or use tax shall not be allowed unless:~~

- ~~1. The qualified person furnishes the retailer with a manufacturer's exemption certificate no later than 60 days after the date of the purchase; and~~
- ~~2. The retailer timely files a sales and use tax return claiming the partial exemption and, together with that timely return, provides the Board with a copy of the manufacturer's exemption certificate.~~

~~(B) Exclusions. Except as provided in subdivision (f)(1)(C) below, retailers claiming the partial exemption in timely filed returns will not be required to furnish the Board with copies of manufacturer's exemption certificates for sales or leases of tangible personal property made by a retailer at any single physical location to a single qualified purchaser that do not exceed an aggregate total of \$25,000 during a single calendar quarter. Regardless of the total quarterly sales per purchaser, however, when necessary for the efficient administration of the sales and use tax law, the Board may, on 30 days' written notice, require a retailer to commence furnishing the Board with copies of all certificates on a quarterly basis pursuant to subdivision (f)(1)(A)2.~~

~~(C) Retention and Availability of Certificates. A retailer must retain each manufacturer's exemption certificate received from a qualified person for a period of four years from the date on which the retailer claims a partial exemption based on the exemption certificate.~~

Within 45 days of the Board's request, retailers must furnish to the Board any and all manufacturer's exemption certificates, or copies thereof, received from qualified persons, including exemption certificates for aggregate sales or leases of \$25,000 or less to a single qualified person made at any single physical location of the retailer during a single calendar quarter.

(2) ~~Manufacturer's Use Tax Declaration.~~ Except as provided in section 6902.2 of the Revenue and Taxation Code, a partial exemption from the use tax shall not be allowed unless the qualified person:

(A) ~~Timely files a sales and use tax return or consumer use tax return for the period in which the purchase occurs and timely pays any applicable tax in full that is excluded from this partial exemption as provided in subdivision (c) of this regulation; and~~

(B) ~~Attaches a completed manufacturer's use tax declaration to the sales and use tax return or consumer use tax return that is timely filed with the Board.~~

(3) ~~Refund of Partial Exemption.~~

(A) ~~For the period commencing on January 1, 1994, and ending on December 31, 1994, a qualified person may claim the partial exemption on qualified purchases from an in-state retailer or an out-of-state retailer obligated to collect the use tax by furnishing the retailer with a manufacturer's exemption certificate on or before March 31, 1995. The retailer must refund the tax directly to the purchaser or, at the purchaser's sole option, the purchaser may be credited with such amount. In the event that the retailer has already reported and paid the tax to the Board, the retailer must file a written claim for refund on or before April 30, 1995.~~

(B) ~~A person who paid sales tax on a qualified sale or paid use tax on a qualified purchase and who failed to claim the partial exemption as provided by this regulation may file a claim for refund equal to the amount of the partial exemption that he or she could have claimed pursuant to this regulation. The procedure for such a claim shall be the same as for other claims for refund filed pursuant to Revenue and Taxation Code section 6901. For transactions subject to use tax, a person filing a claim for refund of the partial exemption has the burden of establishing that he or she was entitled to claim the partial exemption with respect to the amount of refund claimed under this part. For transactions subject to sales tax, a person filing a claim for refund of the partial exemption has the burden of establishing that the purchaser of the qualified property otherwise met all the requirements of a qualified person at the time of the purchase subject to the refund claimed under this part.~~

(4) ~~Construction Contractors.~~ In the case of a contractor who purchases property as an agent of a qualified person or for subsequent resale to a qualified person, the qualified person is deemed to be the purchaser for purposes of this subdivision.

~~(g) Conversion of Property to a Use Not Qualifying for the Partial Exemption. Notwithstanding subdivision (a), this partial exemption shall not apply to any sale of, or the storage, use, or other consumption in this state of property that, within one year from the later of the date of purchase of the property or the date that the property was first placed into service by the purchaser in an exempt use, is: (i) removed from this state, (ii) converted from an exempt use under this regulation to some other use not qualifying for the partial exemption, or (iii) used in a manner not qualifying for the partial exemption under this regulation. For purposes of this subdivision, property is converted to a use not qualifying for the partial exemption if, without limitation, the property, or any interest in the property, or possession or control of the property, is either directly or indirectly sold, transferred, leased, or assigned to a person who is not a qualified person on the date the property is sold, transferred, leased, or assigned to such non-qualified person. In the case of a corporation that, as a qualified person, purchases tangible personal property under this partial exemption and then, within one year from the later of the date of purchase of the property or the date that the property was first placed into service by that corporation in an exempt use, either directly or indirectly transfers that property to its parent corporation that is not a qualified person on the date of the transfer of property to the parent corporation, that property has been converted to a use not qualifying for the partial exemption.~~

~~(h) Purchaser's Liability for the Payment of Sales Tax. If a purchaser submits a copy of a manufacturer's exemption certificate to the seller, and then within one year from the later of the date of purchase of the property or the date that the property was first placed into service by the purchaser in an exempt use, the purchaser either (i) removes that property from this state, (ii) converts that property from an exempt use under this regulation to some other use not qualifying for the partial exemption, or (iii) uses that property in a manner not qualifying for the partial exemption under this regulation, then, in that event, the purchaser shall be liable for payment of sales tax, with applicable interest, to the same extent as if the purchaser were a retailer making a retail sale of the property at the time the property was so removed, converted, or used; and the sales price of the property to the purchaser shall be deemed to be the gross receipts from that retail sale. For purposes of this subdivision, property is converted to a use not qualifying for the partial exemption if, without limitation, the property, or any interest in the property, or possession or control of the property, is either directly or indirectly sold, transferred, leased, or assigned to a person who is not a qualified person on the date the property is sold, transferred, leased, or assigned to such nonqualified person.~~

~~(i) Leases to Qualifying Persons.~~

~~(1) Leases—In General. Subject to all the limitations and conditions set forth in this regulation and regulation 1525.3, this partial exemption may apply to rental receipts paid by a qualified person with respect to a lease of tangible personal property to the qualified person, which tangible personal property is used as set forth in subdivisions (a)(1), (a)(2), (a)(3), or (a)(4) of this regulation.~~

~~(2) Leases—Acquisition Sale and Leaseback. A person will be regarded as having paid sales tax reimbursement or use tax with respect to that person's purchase of property, within the meaning of those words as they are used in section 6010.65 of the Revenue and Taxation~~

~~Code, if the person has paid all applicable taxes with respect to the acquisition of the property, notwithstanding the fact that the sale and purchase of the property may have been subject to the partial exemption from tax provided by this regulation.~~

~~(3) Subsequent Lease of Property Acquired Subject to Partial Exemption. If a person has acquired property subject to the partial exemption provided by this regulation and has paid all applicable taxes at that acquisition, the property will be regarded as property as to which sales tax reimbursement or use tax has been paid, and the subsequent lease of that property will not be subject to tax measured by rental receipts.~~

~~(j) Operative Date. Except as expressly set forth otherwise in subdivisions (c)(6)(A)6. and (e) of this regulation, this regulation is operative as of January 1, 1994. All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or a use made after December 31, 2003.~~

~~Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Section 6377, Revenue and Taxation Code.~~

Appendix A

SECTION 6377 MANUFACTURER'S EXEMPTION CERTIFICATE

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

PLEASE NOTE

This exemption being declared applies only to the state use tax which is at the rate of 5% effective January 1, 2002, 4.75% from January 1, 2001 to December 31, 2001, and 5% from January 1, 1995 to December 31, 2000, and is specific to this transaction only and may not be construed to exempt other transactions. As the purchaser, you remain liable for the applicable local and district taxes. To claim the exemption, this declaration must accompany a timely filed sales and use tax return for the period of purchase. Void after expiration date. Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or a use made after December 31, 2003. Questions regarding this certificate should be directed to: [insert contact information]

Certificate No:
Valid Period Begins:
Valid Period Expires:
(*See below for leases)

I hereby certify that the tangible personal property described below and purchased or leased from:
(enter seller's/lessor's name and address)

SELLER'S NAME _____

SELLER'S ADDRESS (Street, City, State, Zip Code) _____

and will be used by me primarily (please check one)

- 1. for manufacturing, processing, refining, fabricating, or recycling, or
- 2. for research and development activities as described in Internal Revenue Code Section 174, or
- 3. to maintain, repair, measure, or test any property being used for (1) or (2) above, at my facility located

at (enter facility's address): _____
(Street, City, State, Zip Code)

SALES INVOICE NUMBER	SALES INVOICE DATE	DESCRIPTION OF QUALIFIED PROPERTY PURCHASED OR LEASED*	SALES PRICE/ RENTALS PAYABLE

I understand that if such property is, within one year from the date of purchase or lease, removed from California or converted for use or otherwise used in a manner not qualifying for the partial exemption that I am required by the Sales and Use Tax Law to report and pay the state tax measured by the sales price/rentals payable of the property to/by me. Taxable rentals payable from the lease of certain tangible personal property to a qualified person are subject to the partial exemption for a period of six years from the date of inception of the lease. The lease must commence during the time in which this Certificate is valid. *Attach a copy of the lease agreement.

PRINT NAME OF PURCHASER OR PURCHASER'S AUTHORIZED REPRESENTATIVE	TITLE	
SIGNATURE	DATE	PERMIT NUMBER

****NOT VALID UNLESS COMPLETED BY THE CALIFORNIA STATE BOARD OF EQUALIZATION**

The following business has been registered as a "qualified person" who has certified that this purchase/lease of tangible personal property will be used in a manner entitling them to the exemption provided in Section 6377 of the Revenue and Taxation Code.

BUSINESS NAME	SIC CODE
BUSINESS ADDRESS (Street, City, State, Zip Code)	PERMIT NUMBER

****AUTHORIZED BY: (Must be signed by two Board representatives)**

REVIEWED BY	DATE
APPROVED BY	DATE

**** WHEN COMPLETED AND SIGNED, THIS FORM MAY BE REPRODUCED FOR USE BY THE QUALIFIED PERSON LISTED ABOVE**

Appendix B

SECTION 6377 MANUFACTURER'S USE TAX DECLARATION

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

PLEASE NOTE

This is a partial exemption from sales and use taxes at the rate of 5% effective January 1, 2002, 4.75% from January 1, 2001 to December 31, 2001, and 5% from January 1, 1995 to December 31, 2000. You are not relieved from your obligations for the local and district taxes on this transaction. The exemption is specific to this transaction only and may not be construed to exempt other transactions. Generally, the partial exemption will not be allowed unless this certificate is issued within 60 days after the date of purchase and the retailer claims the exemption on a timely filed return. Void after expiration date. Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for sales made after December 31, 2003. Questions regarding this certificate should be directed to: [insert contact information]

Certificate No:

Valid Period Begins:

Valid Period Expires:

(*See below for leases)

I hereby certify that the tangible personal property described below that is subject to use tax was purchased or is being leased from: (enter seller's/lessor's name and address)

SELLER'S NAME

SELLER'S ADDRESS (Street, City, State, Zip Code)

and will be used by me primarily (please check one)

- 1. for manufacturing, processing, refining, fabricating, or recycling, or
- 2. for research and development activities as described in Internal Revenue Code Section 174, or
- 3. to maintain, repair, measure, or test any property being used for (1) or (2) above, at my facility located at (enter facility's address):

(Street, City, State, Zip Code)

SALES INVOICE NUMBER	SALES INVOICE DATE	DESCRIPTION OF PROPERTY PURCHASED OR LEASED*	SALES PRICE/ RENTALS PAYABLE

I understand that if such property is, within one year from the date of purchase or lease, removed from California or converted for use or otherwise used in a manner not qualifying for the partial exemption that I am required by the Sales and Use Tax Law to report and pay the state tax measured by the sales price/rentals payable of the property to/by me. Taxable rentals payable from the lease of certain tangible personal property to a qualified person are subject to the partial exemption for a period of six years from the date of inception of the lease. The lease must commence during the time in which this Certificate is valid. *Attach a copy of the lease agreement.

PRINT NAME OF PURCHASER OR PURCHASER'S AUTHORIZED REPRESENTATIVE	TITLE	
SIGNATURE	DATE	PERMIT NUMBER

**** NOT VALID UNLESS COMPLETED BY THE CALIFORNIA STATE BOARD OF EQUALIZATION**

The following business has been registered as a "qualified person" who has certified that this purchase/lease of tangible personal property will be used in a manner entitling them to the exemption provided in Section 6377 of the Revenue and Taxation Code.

BUSINESS NAME	SIC CODE
BUSINESS ADDRESS (Street, City, State, Zip Code)	PERMIT NUMBER

****AUTHORIZED BY: (Must be signed by two Board representatives)**

REVIEWED BY	DATE
APPROVED BY	DATE

** WHEN COMPLETED AND SIGNED, THIS FORM MAY BE REPRODUCED FOR USE BY THE QUALIFIED PERSON LISTED ABOVE

Text of Proposed Changes to

Title 18. Public Revenue

~~1525.3. Manufacturing Equipment—Leases of Tangible Personal Property.~~

~~(a) General Application to Leases. Leases of tangible personal property which are classified as “continuing sales” and “continuing purchases” of tangible personal property, in accordance with Regulation 1660, “Leases of Tangible Personal Property—In General,” may qualify for the partial exemption from tax for manufacturing equipment, under the conditions set forth in paragraph (i)(1) of Regulation 1525.2, “Manufacturing Equipment.” Lease transactions which qualify for the partial exemption are taxed at the rate specified in Regulation 1525.2, paragraph (a).~~

~~(b) Recharacterization. With respect to transactions which the parties denominate as a “lease,” but which are recharacterized for sales and use tax purposes either as sales at their inception, pursuant to Regulation 1641, “Credit Sales and Repossessions,” paragraph (b), or as sales under a security agreement, Regulation 1660, “Leases of Tangible Personal Property—In General,” paragraph (a)(2), the transactions may qualify for the partial exemption, in accordance with Regulation 1525.2.~~

~~(c) Continuation of Partial Exemption. Where possession of tangible personal property is transferred to a qualified person as defined in paragraphs (c) and (d) of Regulation 1525.2 and pursuant to a lease agreement classified as a continuing sale and continuing purchase, lease receipts shall remain partially exempt for a period of six years from the date of the inception of the lease whether or not the lessee remains as a qualified person throughout the six year period. At the close of the six year period from the date of the inception of the lease, lease receipts are subject to tax without exemption.~~

~~(d) Leases of Tax Paid Property. The partial exemption is not available to lessors who lease to qualified persons or to vendors to such lessors when the lessor elects to pay sales tax reimbursement at the time of acquisition of the property or pays use tax measured by the purchase price of the property.~~

~~(e) Manufacturers Who Lease Qualified Property. A lease of tangible personal property by the manufacturer of that property is ordinarily regarded as a “continuing sale” and “continuing purchase” in accordance with Regulation 1660, “Leases of Tangible Personal Property—In General.” Nevertheless, beginning January 1, 1997, a lessor of tangible personal property described in sections 17053.49 or 23649 of the Revenue and Taxation Code, who is the manufacturer of that property and who leases that property to a qualified person, as defined in section 17053.49 or 23649 of the Revenue and Taxation Code, in a form that is not substantially the same form as acquired, may, in lieu of reporting tax measured by the rentals payable, elect to pay tax measured by the cost price of that property where the election is made on or before the due date of the return for the period in which the property is first leased to the qualified person. The election shall be made by reporting use tax measured by the cost price of that property on the return for that period. The election shall not be revoked with respect to the property as to which it is made. The lease of that property for which an election is made to report and pay tax on the cost price of that property shall thereafter be excluded from the classification of a “continuing sale” and “continuing purchase.”~~

For purposes of this subdivision, "cost price" means the price at which similar property has been previously sold or offered for sale. If that property has not been previously sold or offered for sale, then the cost price shall be deemed to be the aggregate of the following:

~~(1) Cost of materials.~~

~~(2) Direct labor.~~

~~(3) The pro rata share of all overhead costs attributable to the manufacturer of the property.~~

~~(4) Reasonable profit from the manufacturing operations which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the factors listed in subsections (1) to (3), inclusive.~~

~~(f) Operative Date. All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or use made after December 31, 2003.~~

~~Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6244.5 and 6377, Revenue and Taxation Code.~~

CHANGES WITHOUT REGULATORY EFFECT UNDER
CALIFORNIA CODE OF REGULATIONS, TITLE 1, SECTION 100

Statement of Explanation

Title 18. Public Revenues

Regulations 1525.2, *Manufacturing Equipment*, and
1525.3, *Manufacturing Equipment - Leases of Tangible Personal Property*

A. Factual Basis

The State Board of Equalization (Board) adopted California Code of Regulations, title 18, sections (Regulations) 1525.2, *Manufacturing Equipment*, and 1525.3, *Manufacturing Equipment - Leases of Tangible Personal Property*, to implement, interpret, and make specific the provisions of Revenue and Taxation Code section 6377, which provided a partial exemption from sales and use tax for certain property purchased by a qualified person to be used primarily in specified activities, including manufacturing. Section 6377 was added to the Revenue and Taxation Code by Statutes 1993, chapter 881 (Sen. Bill No. 671), section 1 and last amended by Statutes 1996, chapter 954 (Sen. Bill No. 38), section 6 before section 6377 was repealed by its own terms, effective January 1, 2004.¹ Therefore, there has not been any statutory authority for the partial exemption implemented, interpreted, and made specific by Regulations 1525.2 and 1525.3 since January 1, 2004. And, as a result, the Board proposes to repeal Regulations 1525.2 and 1525.3 under California Code of Regulations, title 1, section (Rule) 100 and thereby delete the regulations, including appendices A and B to Regulation 1525.2, from the California Code of Regulations. The proposed deletion of Regulations 1525.2 and 1525.3 from the California Code of Regulations is appropriate for processing under Rule 100 because Rule 100, subdivision (a)(2), specifically provides that deleting a regulatory provision for which all statutory authority has been repealed is a change without regulatory effect.

B. Proposed Changes

The following Rule 100 changes are proposed to repeal Regulations 1525.2 and 1525.3, including appendices A and B to Regulation 1525.2, and thereby delete the regulations from the California Code of Regulations:

¹ Section 6377, subdivision (g)(2)(A) provided that the "section shall cease to be operative on January 1, 2001, or on January 1 of the earliest year thereafter, if the total employment in this state, as determined by the Employment Development Department on the preceding January 1, does not exceed by 100,000 jobs the total employment in this state on January 1, 1994." This contingency was met on January 1, 2003, and the section was therefore repealed on the subsequent January 1, which was January 1, 2004.

TEXT OF PROPOSED CHANGES

Regulation 1525.2. Manufacturing Equipment.

(a) ~~Partial Exemption for Property Purchased for Use in the Manufacturing Process. Section 6377 of the Revenue and Taxation Code provides a partial exemption from sales and use tax for certain properties described in this regulation.~~

~~For the period commencing on January 1, 1994, and ending on December 31, 1994, the partial exemption applies to the taxes imposed by the state (6%), but does not apply to the taxes imposed by counties, cities, and districts pursuant to the Bradley Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code § 7200, et seq.) or the Transactions and Use Tax Law (Rev. & Tax. Code §§ 7251, et seq.).~~

~~For the period commencing on January 1, 1995, and ending on December 31, 2000, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2001, and ending on December 31, 2001, the partial exemption applies to the taxes imposed by sections 6051 and 6201 of the Revenue and Taxation Code (4.75%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2002, and ending on December 31, 2003, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~Pursuant to the provisions of the Revenue and Taxation Code section 6377(g), the partial exemption from tax on the sale and use of property used in manufacturing and related activities as described in this regulation expired on December 31, 2003.~~

~~Subject to the limitations set forth above, this partial exemption applies to gross receipts from the sale, storage, use, or other consumption in this state of the following items:~~

- ~~(1) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point that raw materials are received by the qualified person and introduced into the process and ending at the point at which the property has been altered to its completed form, including packaging, if required. For purposes of this regulation:~~

~~(A) Raw materials will be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified person's manufacturing activities are conducted. Raw materials that are stored on premises other than where the qualified person's manufacturing activities are conducted, however, will not be considered to have been introduced into the process for purposes of this regulation.~~

~~(B) For purposes of this regulation, the term "packaging" includes only that packaging necessary to prepare the goods for delivery to and placement in the qualified person's finished goods inventory, or to prepare the goods so that they are suitable for delivery to and placement in finished goods inventory. Any additional packaging, such as that packaging necessary to consolidate the goods prior to shipping or to protect them during transportation, shall not be considered to be "packaging" for purposes of this regulation.~~

~~(2) Tangible personal property purchased for use by a qualified person to be used primarily in research and development as defined in subdivision (c)(8).~~

~~(3) Tangible personal property purchased for use by a qualified person to be used primarily to maintain, repair, measure, or test any property described in subdivision (a)(1) or (a)(2).~~

~~(4) Tangible personal property purchased for use by a contractor purchasing that property either as an agent of a qualified person or for the contractor's own account and subsequent resale to a qualified person for use in the performance of a construction contract for the qualified person who will use the tangible personal property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, or as a research or storage facility for use in connection with the manufacturing process.~~

~~(b) Property Used Primarily in Administration, General Management, or Marketing.~~

~~Notwithstanding any other provision of this regulation, this partial exemption shall not apply to any tangible personal property that is used primarily in administration, general management, or marketing. For purposes of this subdivision:~~

~~(1) Tangible personal property is used primarily in administration, general management, or marketing when it is used 50 percent or more of the time in one or more of those activities.~~

~~(2) Tangible personal property used primarily to clean and maintain the factory floor of a manufacturing facility is used primarily in a stage of the manufacturing of property and is not used primarily in administration, general management, or marketing.~~

~~(3) Fire safety equipment that is tangible personal property and that is used primarily at and in connection with the factory floor of a manufacturing facility is used primarily in a stage of the manufacturing of property and is not used primarily in administration, general management, or marketing.~~

~~(c) Definitions. For purposes of this regulation:~~

(1) “Fabricating” means to make, build, create, produce, or assemble components or property to work in a new or different manner.

(2) “Manufacturing” means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or for use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property. For purposes of this regulation, “greater functionality” means that the tangible personal property has been improved so that it can perform new or different functions than the original property. Manufacturing includes logging, that is, the felling of timber, but does not include tree farming. Manufacturing does not include crop harvesting. Provided that the activity constitutes a “sale” as that term is used in subdivision (b) of section 6006 of the Revenue and Taxation Code, the tangible personal property need not be owned by the qualified person in order for the activity to qualify as manufacturing for purposes of this regulation.

(3) “Primarily” means that the tangible personal property is used 50 percent or more of the time in the designated activity or activities.

(4) “Process” means the period beginning at the point at which any raw materials are received by the qualified person and are introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified person and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified person has altered tangible personal property to its completed form including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified person's manufacturing, processing, refining, or recycling activity is conducted. Raw materials that are stored on premises other than where the qualified person's manufacturing, processing, refining, fabricating, or recycling activity is conducted, shall not be considered to have been introduced into the manufacturing, processing, refining, fabricating, or recycling process.

(5) “Processing” means the physical application of materials and labor to modify or change the characteristics of property.

(6) “Qualified person” means any person that satisfies the requirements of both subdivisions (c)(6)(A) and (c)(6)(B) below with regard to the trade or business in which the property will be placed into service in the use qualifying the property for this partial exemption:

(A) A “qualified person” must have first commenced trade or business activities in a new trade or business in this state on or after January 1, 1994. For purposes of this subdivision, the term “activities” means trade or business activities. In determining whether or not a person is qualified within the meaning of this subdivision, the following rules apply:

1. The term “trade or business activities” does not mean the mere formation or organization of a corporation or other business entity that is intended to conduct a

~~trade or business. Instead, a corporation or business entity first conducts activities when it first starts or commences the trade or business for which it was organized. The acquisition of operating assets that are necessary to the type of business contemplated, however, will constitute commencing activities. The term "operating assets" as used in this subdivision means assets that are in a state of readiness to be placed in service within a reasonable time period following their acquisition.~~

~~2. Notwithstanding any other provision of this subdivision, a person will not be considered to have first commenced activities in a new trade or business in this state on or after January 1, 1994, if, at any time within the 36 months preceding that date, that person, or any related person, was required to have secured a seller's permit under section 6066 of the Revenue and Taxation Code for that trade or business, or any other trade or business classified under the same division of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition (the "Manual"). For purposes of this regulation, the term "division" means a division as that term is used in the Manual.~~

~~3. A trade or business is not a new trade or business in this state if, within the 36 months preceding the date that activities were first commenced in that trade or business in this state, either the person claiming the partial exemption, or any related person, had conducted any activities in this state in any trade or business classified under the same division of the Manual as that trade or business.~~

~~4. Where a person, or any related person, is engaged in one or more trade or business activities in this state, or has been engaged in one or more trade or business activities in this state within the preceding 36 months (a "prior trade or business activity"), and thereafter commences an additional trade or business activity in this state, the additional trade or business activity shall only be treated as a new trade or business if the additional trade or business activity is classified under a different division of the Manual than are any of the person's (or any related person's) current or prior trade or business activities in this state within the preceding 36 months.~~

~~5. Where a person, including all related persons, is engaged in trade or business activities wholly outside of this state and that person first commences doing business in this state (within the meaning of section 23101 of the Revenue and Taxation Code) after December 31, 1993 (other than by purchase or other acquisition described in subdivision (c)(6)(A)6., the newly commenced trade or business activity in this state shall be treated as a new trade or business for purposes of this subdivision.~~

~~6. On or after January 1, 1995, notwithstanding anything else set forth in this subdivision, in any case where a person purchases or otherwise acquires all or any portion of the assets of an existing trade or business (irrespective of the form of the entity) that is doing business in this state (within the meaning of section 23101 of the Revenue and Taxation Code), the trade or business thereafter conducted by that person (or any related person) shall not be treated as a new trade or business if the aggregate fair market value of the acquired assets (including real, personal, tangible,~~

and intangible property) used by that person (or any related person) in the conduct of his or her trade or business exceeds 20 percent of the aggregate fair market value of the total assets of the person (or any related person) being used in the same trade or business both within and without this state. For purposes of this subdivision only:

a. The determination of the relative fair market values of the acquired assets and the total assets shall be made as of the last day of the month following the quarterly period in which the person (or any related person) first uses any of the acquired trade or business assets in his or her business activity.

b. Any acquired assets that constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the transferor shall not be treated as assets acquired from an existing trade or business, unless those assets also constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the acquiring person (or any related person).

c. The trade or business conducted in this state by the acquiring person after the asset acquisition date shall be considered to be the same as an out-of-state trade or business conducted or previously conducted by the acquiring person (or any related person) only if the trade or business activities of both companies are or would be classified in the same division of the Manual.

d. An acquired trade or business will not be considered to have been acquired as an existing trade or business for purposes of this subdivision if it is acquired either: (1) from a liquidation sale of assets pursuant to a bankruptcy filed under Chapter 7 of the United States Bankruptcy Code; or (2) pursuant to a creditor's execution or foreclosure sale of a secured interest in the assets of the trade or business.

e. Example No. 1: Corporation X is doing business wholly outside of this state in the trade or business of manufacturing automobiles. The total fair market value of the total assets of this trade or business is \$100,000,000. Then, on or after January 1, 1994, Corporation X acquires all of the assets of an automobile manufacturing business in this state with a fair market value of \$5,000,000 and immediately uses the acquired assets in its automobile manufacturing trade or business. Thereafter, between the date of acquisition and the last day of the month following the quarterly period during which the acquisition occurred, Corporation X acquires another \$1,000,000 in assets for use in the automobile manufacturing business in this state. Under these assumed facts, the conditions set forth in this subparagraph will not serve to disqualify Corporation X from the partial exemption since the fair market value of the acquired assets does not exceed 20 percent ($\$5,000,000/\$106,000,000$) of the aggregate fair market value of the total assets of the trade or business being conducted by Corporation X; and neither Corporation X nor any related person had conducted any trade or business activities in this state within the preceding 36 months.

f. Example No. 2: Assume the same facts as in Example No. 1 above, but in this case, prior to acquiring the assets of the automobile manufacturing business in this state, Corporation X was solely and exclusively in the trade or business of providing data processing services. After the acquisition of the assets by Corporation X, however, the acquired assets will continue to be used in the automobile manufacturing business in this state. Assume further that no additional purchases are made after the date of acquisition. Under these assumed facts, since data processing services and automobile manufacturing are classified in different divisions of the Manual, the partial exemption will not be available to Corporation X because the fair market value of the acquired assets exceeds 20 percent ($\$5,000,000/\$5,000,000$) of the aggregate fair market value of the total assets held by Corporation X in the same trade or business.

7. In any case where the legal form under which a trade or business activity is being conducted is changed, the change in form shall be disregarded and the determination of whether the trade or business activity is a new business shall be made by treating the person as having purchased or otherwise acquired all or any portion of the assets of an existing trade or business. For purposes of this subdivision only:

a. Example No. 1: Corporation X is doing business in this state. One of its trade or business activities in this state is manufacturing automobiles. After January 1, 1994, for consideration, Corporation X transfers all of the assets used in the trade or business of manufacturing automobiles to a newly formed, wholly owned subsidiary known as Corporation Y. For purposes of applying this regulation, this transaction shall be treated as an acquisition of an existing trade or business by Corporation Y.

b. Example No. 2: Partnership A is a manufacturer doing business in this state. After January 1, 1994, for consideration, Partnership A transfers all of its assets to a newly formed corporation known as Corporation B. Corporation B is owned by the partners of Partnership A in the same proportionate ownership interests as their respective ownership interests in the partnership. For purposes of applying this regulation, this transaction shall be treated as an acquisition of an existing trade or business by Corporation B.

8. For purposes of this subdivision, a person is a "related person" if that person is or previously was related to the qualified person within the meaning of either section 267 or 318 of the Internal Revenue Code.

9. The term "acquire" shall include any gift, inheritance, transfer incident to divorce, or any other transfer, whether or not for consideration.

(B) A qualified person must be engaged in those manufacturing lines of business described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition. For purposes of this subdivision:

1. For purposes of classifying a line or lines of business, the economic unit shall be the “establishment” and the classification of the line or lines of business will be based on the establishment's single most predominant activity based upon value of production. The term “establishment” means an economic unit, generally at a single physical location, where business is conducted or where services or manufacturing or other industrial operations are performed. The following will generally constitute an “establishment”: a factory, mill, store, hotel, movie theater, mine, farm, ranch, bank, railroad depot, airline terminal, sales office, warehouse, or central administrative office.

2. For purposes of determining the “establishment” or “establishments” of a trade or business:

a. Where distinct and separate economic activities are performed at a single physical location, such as construction activities operated out of the same physical location as a lumber yard, each activity should be treated as a separate establishment where: (i) no one industry description in the classification includes such combined activities; (ii) the employment in each such economic activity is significant; and (iii) separate reports are prepared on the number of employees, their wages and salaries, sales or receipts, property and equipment, and other types of financial data, such as financial statements, job costing, and profit center accounting. For purposes of this paragraph, whether or not employment in an economic activity is significant shall be based upon all of the facts and circumstances. Nevertheless, employment in an economic activity will be considered to be “significant” for purposes of this paragraph whenever more than 25 percent of the taxpayer's total number of employees at a single physical location, or more than 25 percent of the taxpayer's total dollar value of payroll at a single physical location, is attributable to the economic activity being tested for separate establishment status.

b. An establishment is not necessarily identical with the enterprise or company which may consist of one or more establishments. Also, an establishment is to be distinguished from subunits of the establishment such as departments.

c. Where a person conducts business at more than one establishment within the meaning of this subdivision, then that person shall be considered to be a “qualified person” for purposes of this regulation only as to those purchases that are intended to be used and are actually used in those lines of business that are described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition.

(7) “Refining” means the process of converting a natural resource to an intermediate or finished product.

~~(8) “Research and development” means those activities that are described in section 174 of the Internal Revenue Code or in any regulations thereunder.~~

~~(9) “Tangible personal property” does not include any of the following:~~

~~(A) Real property, including tangible personal property to be incorporated into an improvement to real property, except for “special purpose buildings and foundations” as defined in subdivision (c)(10)(D) and conveyance systems and assembly lines as provided in subdivision (c)(10)(A).~~

~~(B) Consumables with a normal useful life of less than one year, except as provided in subdivision (c)(10)(E). For purposes of this regulation, it shall be presumed tangible personal property that the qualified person treats as having a normal useful life of less than one year for state income or franchise tax purposes is tangible personal property with a normal useful life of less than one year. This presumption may be rebutted by evidence satisfactory to the Board.~~

~~(C) Furniture, inventory, equipment used in the extraction process, equipment used to store raw materials that have not yet entered or commenced the manufacturing process, or equipment used to store finished products that have completed the manufacturing process. The extraction process includes such severance activities as mining, oil and gas extraction.~~

~~(D) Any property for which a credit is claimed under either section 17053.49 or 23649 of the Revenue and Taxation Code.~~

~~(10) “Tangible personal property” includes but is not limited to the following:~~

~~(A) Machinery and equipment within the meaning of subdivision (a)(6) of Regulation 1521 of the Sales and Use Tax Regulations, including component parts and contrivances such as belts, shafts, moving parts, and operating structures. The term also includes conveyance systems and assembly lines without regard to the manner of affixation to real property.~~

~~(B) All equipment or devices used or required to operate, control, regulate, or maintain the machinery, including, without limitation, computers, data processing equipment, and computer software, including both operating programs and application programs, together with all repair and replacement parts with a useful life of one or more years therefor, whether purchased separately or in conjunction with a complete machine and regardless of whether the machine or component parts are assembled by the taxpayer or another party. Any repair and replacement parts that the qualified person treats as having a useful life of less than one year for state income or franchise tax purposes shall be presumed to have a useful life of less than one year for purposes of this regulation. This presumption may be rebutted by evidence satisfactory to the Board.~~

~~(C) Property used in pollution control that meets or exceeds standards established by this state or any local or regional governmental agency within this state.~~

~~(D) Special purpose buildings and foundations that (i) are used as an integral part of the manufacturing, processing, refining, or fabricating process, or (ii) constitute a research facility used during the manufacturing process as an integral part of a manufacturing, processing, refining, or fabricating activity, or (iii) constitute a storage facility used during the manufacturing process as an integral part of a manufacturing, processing, refining, or fabricating activity. For purposes of this subdivision:~~

~~1. For purposes of this subdivision, “special purpose building and foundation” means only a building and the foundation immediately underlying the building that is specifically designed and constructed or reconstructed for the installation, operation, and use of specific machinery and equipment with a special purpose, which machinery and equipment, after installation, will become affixed to or a fixture of the real property, and the construction or reconstruction of which is specifically designed and used exclusively for the specified purposes as set forth in subdivision (a)(1) of this regulation (the qualified purpose).~~

~~2. A building is specifically designed and constructed or modified for a qualified purpose if it is not economic to design and construct the building for the intended purpose and then use the structure for a different purpose.~~

~~3. A building is used exclusively for a qualified purpose only if its use does not include a use for which it was not specifically designed and constructed or modified. Incidental use of a building for non-qualified purposes does not preclude the building from being a special purpose building. “Incidental use” means a use which is both related and subordinate to the qualified purpose. A use is not subordinate if more than one third of the total usable volume of the building is devoted to a use which is not a qualifying purpose.~~

~~4. In the event an entire building does not qualify as a special purpose building, a taxpayer may establish that a portion of a building, and the foundation immediately underlying the portion, qualifies for treatment as a special purpose building and foundation if the portion satisfies all of the definitional provisions in this subdivision.~~

~~5. Buildings and foundations that do not meet the definition of a special purpose building and foundation set forth above include, but are not limited to, buildings designed and constructed or reconstructed principally to function as a general purpose manufacturing, industrial, or commercial building; research facilities that are used primarily prior to or after, or prior to and after, the manufacturing process; or storage facilities that are used primarily prior to or after, or prior to and after, completion of the manufacturing process.~~

~~6. For purposes of this subdivision, the term “integral part” means that the special purpose building or foundation (i) is used directly in the activity qualifying for the~~

partial exemption from sales and use tax and (ii) is essential to the completeness of that activity. In determining whether property is used as an integral part of manufacturing, all properties used by the qualified person in processing the raw materials into the final product are properties used as an integral part of manufacturing.

(E) Fuels used or consumed in the manufacturing process.

(F) Property used in recycling.

(11) "Standard Industrial Classification" means a Standard Industrial Classification in the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition.

(d) ~~Three Year Limitation.~~ Notwithstanding any other provision of this regulation, once a person has conducted business activities in a new trade or business for three or more years, that person will no longer be considered to be in a "new trade or business," nor "qualified" for this partial exemption.

(e) ~~Taxes as to Which the Partial Exemption Does Not Apply.~~ This partial exemption does not apply to any tax levied by a county, city, or district pursuant to, or in accordance with, either the Bradley Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code §§7200 et seq.) or the Transactions and Use Tax Law (Rev. & Tax Code §§7251 et seq.).

On or after January 1, 1995, this partial exemption shall not apply to any tax levied pursuant to section 6051.2 and 6201.2 of the Revenue and Taxation Code, or pursuant to section 35 of article XIII of the California Constitution.

(f) ~~Exemption Certificates.~~ Except as otherwise set forth in subdivision (f)(3), to claim the partial exemption provided by this regulation, a person must be both pre-qualified by the Board and either registered to hold a seller's permit or maintain a consumer use tax account. Exemption certificates issued to qualified persons will contain a control number and expiration date for verifying a person's status as a qualified person. An exemption certificate is not valid if it has not been issued by the Board or if it is accepted after the expiration date on the certificate. Qualified persons who have been pre-qualified may reproduce the issued certificates as needed for their qualifying purchases.

The exemption certificates issued by the Board will be in substantially the same form as they appear in Appendices A and B of this regulation. Qualified persons who purchase or lease tangible personal property from an in-state retailer or an out-of-state retailer obligated to collect the use tax must provide the retailer with a manufacturer's exemption certificate in order to claim the partial exemption. The manufacturer's use tax declaration must be completed by a qualified person to claim a partial exemption from use tax on purchases of tangible personal property from an out-of-state retailer not obligated to collect the use tax.

Solely for the purposes of this regulation, it is presumed that a seller accepts a manufacturer's exemption certificate from a prequalified purchaser in good faith in the absence of evidence to the contrary. A retailer's direct knowledge that the purchaser is not purchasing tangible personal property for use in a manufacturing activity, that the purchaser intends the tangible personal property for his or her own use, or that the tangible personal property does not have a normal useful life of one year or more constitutes evidence to the contrary. A purchaser providing a manufacturer's exemption certificate accepted in good faith by the seller for tangible personal property that does not qualify for this exemption is liable for the payment of tax as set forth in subdivision (h).

(1) Manufacturer's Exemption Certificates.

(A) In General. Except as otherwise provided in subdivisions (f)(1)(B) or (f)(3) of this regulation, or in section 6902.2 of the Revenue and Taxation Code, a partial exemption from sales or use tax shall not be allowed unless:

1. The qualified person furnishes the retailer with a manufacturer's exemption certificate no later than 60 days after the date of the purchase; and
2. The retailer timely files a sales and use tax return claiming the partial exemption and, together with that timely return, provides the Board with a copy of the manufacturer's exemption certificate.

(B) Exclusions. Except as provided in subdivision (f)(1)(C) below, retailers claiming the partial exemption in timely filed returns will not be required to furnish the Board with copies of manufacturer's exemption certificates for sales or leases of tangible personal property made by a retailer at any single physical location to a single qualified purchaser that do not exceed an aggregate total of \$25,000 during a single calendar quarter. Regardless of the total quarterly sales per purchaser, however, when necessary for the efficient administration of the sales and use tax law, the Board may, on 30 days' written notice, require a retailer to commence furnishing the Board with copies of all certificates on a quarterly basis pursuant to subdivision (f)(1)(A)2.

(C) Retention and Availability of Certificates. A retailer must retain each manufacturer's exemption certificate received from a qualified person for a period of four years from the date on which the retailer claims a partial exemption based on the exemption certificate.

Within 45 days of the Board's request, retailers must furnish to the Board any and all manufacturer's exemption certificates, or copies thereof, received from qualified persons, including exemption certificates for aggregate sales or leases of \$25,000 or less to a single qualified person made at any single physical location of the retailer during a single calendar quarter.

(2) Manufacturer's Use Tax Declaration. Except as provided in section 6902.2 of the Revenue and Taxation Code, a partial exemption from the use tax shall not be allowed unless the qualified person:

~~(A) Timely files a sales and use tax return or consumer use tax return for the period in which the purchase occurs and timely pays any applicable tax in full that is excluded from this partial exemption as provided in subdivision (e) of this regulation; and~~

~~(B) Attaches a completed manufacturer's use tax declaration to the sales and use tax return or consumer use tax return that is timely filed with the Board.~~

~~(3) Refund of Partial Exemption.~~

~~(A) For the period commencing on January 1, 1994, and ending on December 31, 1994, a qualified person may claim the partial exemption on qualified purchases from an in-state retailer or an out-of-state retailer obligated to collect the use tax by furnishing the retailer with a manufacturer's exemption certificate on or before March 31, 1995. The retailer must refund the tax directly to the purchaser or, at the purchaser's sole option, the purchaser may be credited with such amount. In the event that the retailer has already reported and paid the tax to the Board, the retailer must file a written claim for refund on or before April 30, 1995.~~

~~(B) A person who paid sales tax on a qualified sale or paid use tax on a qualified purchase and who failed to claim the partial exemption as provided by this regulation may file a claim for refund equal to the amount of the partial exemption that he or she could have claimed pursuant to this regulation. The procedure for such a claim shall be the same as for other claims for refund filed pursuant to Revenue and Taxation Code section 6901. For transactions subject to use tax, a person filing a claim for refund of the partial exemption has the burden of establishing that he or she was entitled to claim the partial exemption with respect to the amount of refund claimed under this part. For transactions subject to sales tax, a person filing a claim for refund of the partial exemption has the burden of establishing that the purchaser of the qualified property otherwise met all the requirements of a qualified person at the time of the purchase subject to the refund claimed under this part.~~

~~(4) Construction Contractors. In the case of a contractor who purchases property as an agent of a qualified person or for subsequent resale to a qualified person, the qualified person is deemed to be the purchaser for purposes of this subdivision.~~

~~(g) Conversion of Property to a Use Not Qualifying for the Partial Exemption. Notwithstanding subdivision (a), this partial exemption shall not apply to any sale of, or the storage, use, or other consumption in this state of property that, within one year from the later of the date of purchase of the property or the date that the property was first placed into service by the purchaser in an exempt use, is: (i) removed from this state, (ii) converted from an exempt use under this regulation to some other use not qualifying for the partial exemption, or (iii) used in a manner not qualifying for the partial exemption under this regulation. For purposes of this subdivision, property is converted to a use not qualifying for the partial exemption if, without limitation, the property, or any interest in the property, or possession or control of the property, is either directly or indirectly sold, transferred, leased, or assigned to a person who is not a qualified person on the~~

~~date the property is sold, transferred, leased, or assigned to such non-qualified person. In the case of a corporation that, as a qualified person, purchases tangible personal property under this partial exemption and then, within one year from the later of the date of purchase of the property or the date that the property was first placed into service by that corporation in an exempt use, either directly or indirectly transfers that property to its parent corporation that is not a qualified person on the date of the transfer of property to the parent corporation, that property has been converted to a use not qualifying for the partial exemption.~~

~~(h) Purchaser's Liability for the Payment of Sales Tax. If a purchaser submits a copy of a manufacturer's exemption certificate to the seller, and then within one year from the later of the date of purchase of the property or the date that the property was first placed into service by the purchaser in an exempt use, the purchaser either (i) removes that property from this state, (ii) converts that property from an exempt use under this regulation to some other use not qualifying for the partial exemption, or (iii) uses that property in a manner not qualifying for the partial exemption under this regulation, then, in that event, the purchaser shall be liable for payment of sales tax, with applicable interest, to the same extent as if the purchaser were a retailer making a retail sale of the property at the time the property was so removed, converted, or used; and the sales price of the property to the purchaser shall be deemed to be the gross receipts from that retail sale. For purposes of this subdivision, property is converted to a use not qualifying for the partial exemption if, without limitation, the property, or any interest in the property, or possession or control of the property, is either directly or indirectly sold, transferred, leased, or assigned to a person who is not a qualified person on the date the property is sold, transferred, leased, or assigned to such nonqualified person.~~

~~(i) Leases to Qualifying Persons:~~

~~(1) Leases – In General. Subject to all the limitations and conditions set forth in this regulation and regulation 1525.3, this partial exemption may apply to rental receipts paid by a qualified person with respect to a lease of tangible personal property to the qualified person, which tangible personal property is used as set forth in subdivisions (a)(1), (a)(2), (a)(3), or (a)(4) of this regulation.~~

~~(2) Leases – Acquisition Sale and Leaseback. A person will be regarded as having paid sales tax reimbursement or use tax with respect to that person's purchase of property, within the meaning of those words as they are used in section 6010.65 of the Revenue and Taxation Code, if the person has paid all applicable taxes with respect to the acquisition of the property, notwithstanding the fact that the sale and purchase of the property may have been subject to the partial exemption from tax provided by this regulation.~~

~~(3) Subsequent Lease of Property Acquired Subject to Partial Exemption. If a person has acquired property subject to the partial exemption provided by this regulation and has paid all applicable taxes at that acquisition, the property will be regarded as property as to which sales tax reimbursement or use tax has been paid, and the subsequent lease of that property will not be subject to tax measured by rental receipts.~~

~~(j) Operative Date. Except as expressly set forth otherwise in subdivisions (c)(6)(A)6. and (e) of this regulation, this regulation is operative as of January 1, 1994. All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or a use made after December 31, 2003.~~

~~Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Section 6377, Revenue and Taxation Code.~~

Appendix A

SECTION 6377 MANUFACTURER'S EXEMPTION CERTIFICATE

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

PLEASE NOTE

This exemption being declared applies only to the state use tax which is at the rate of 5% effective January 1, 2002, 4.75% from January 1, 2001 to December 31, 2001, and 5% from January 1, 1995 to December 31, 2000, and is specific to this transaction only and may not be construed to exempt other transactions. As the purchaser, you remain liable for the applicable local and district taxes. To claim the exemption, this declaration must accompany a timely filed sales and use tax return for the period of purchase. Void after expiration date. Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or a use made after December 31, 2003. **Questions regarding this certificate should be directed to: [insert contact information]**

Certificate No:
Valid Period Begins:
Valid Period Expires:
(*See below for leases)

I hereby certify that the tangible personal property described below and purchased or leased from:
(enter seller's/lessor's name and address)

SELLER'S NAME _____

SELLER'S ADDRESS (Street, City, State, Zip Code) _____

and will be used by me primarily (please check one)

- 1. for manufacturing, processing, refining, fabricating, or recycling, or
- 2. for research and development activities as described in Internal Revenue Code Section 174, or
- 3. to maintain, repair, measure, or test any property being used for (1) or (2) above, at my facility located _____
at (enter facility's address): _____
(Street, City, State, Zip Code)

SALES INVOICE NUMBER	SALES INVOICE DATE	DESCRIPTION OF QUALIFIED PROPERTY PURCHASED OR LEASED*	SALES PRICE/ RENTALS PAYABLE

I understand that if such property is, within one year from the date of purchase or lease, removed from California or converted for use or otherwise used in a manner not qualifying for the partial exemption that I am required by the Sales and Use Tax Law to report and pay the state tax measured by the sales price/rentals payable of the property to/by me. Taxable rentals payable from the lease of certain tangible personal property to a qualified person are subject to the partial exemption for a period of six years from the date of inception of the lease. The lease must commence during the time in which this Certificate is valid. *Attach a copy of the lease agreement.

PRINT NAME OF PURCHASER OR PURCHASER'S AUTHORIZED REPRESENTATIVE	TITLE	
SIGNATURE	DATE	PERMIT NUMBER

****NOT VALID UNLESS COMPLETED BY THE CALIFORNIA STATE BOARD OF EQUALIZATION**

The following business has been registered as a "qualified person" who has certified that this purchase/lease of tangible personal property will be used in a manner entitling them to the exemption provided in Section 6377 of the Revenue and Taxation Code.

BUSINESS NAME	SIC CODE
BUSINESS ADDRESS (Street, City, State, Zip Code)	PERMIT NUMBER

****AUTHORIZED BY: (Must be signed by two Board representatives)**

REVIEWED BY	DATE
APPROVED BY	DATE

**** WHEN COMPLETED AND SIGNED, THIS FORM MAY BE REPRODUCED FOR USE BY THE QUALIFIED PERSON LISTED ABOVE**

Appendix B

SECTION 6377 MANUFACTURER'S USE TAX DECLARATION

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

PLEASE NOTE

This is a partial exemption from sales and use taxes at the rate of 5% effective January 1, 2002, 4.75% from January 1, 2001 to December 31, 2001, and 5% from January 1, 1995 to December 31, 2000. You are not relieved from your obligations for the local and district taxes on this transaction. The exemption is specific to this transaction only and may not be construed to exempt other transactions. Generally, the partial exemption will not be allowed unless this certificate is issued within 60 days after the date of purchase and the retailer claims the exemption on a timely filed return. Void after expiration date. Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for sales made after December 31, 2003. **Questions regarding this certificate should be directed to: [insert contact information]**

Certificate No:

Valid Period Begins:

Valid Period Expires:

(*See below for leases)

I hereby certify that the tangible personal property described below that is subject to use tax was purchased or is being leased from: (enter seller's/lessor's name and address)

SELLER'S NAME

SELLER'S ADDRESS (Street, City, State, Zip Code)

and will be used by me primarily (please check one)

- 1. for manufacturing, processing, refining, fabricating, or recycling, or
- 2. for research and development activities as described in Internal Revenue Code Section 174, or
- 3. to maintain, repair, measure, or test any property being used for (1) or (2) above, at my facility located at (enter facility's address):

(Street, City, State, Zip Code)

SALES INVOICE NUMBER	SALES INVOICE DATE	DESCRIPTION OF PROPERTY PURCHASED OR LEASED*	SALES PRICE/ RENTALS PAYABLE

I understand that if such property is, within one year from the date of purchase or lease, removed from California or converted for use or otherwise used in a manner not qualifying for the partial exemption that I am required by the Sales and Use Tax Law to report and pay the state tax measured by the sales price/rentals payable of the property to/by me. Taxable rentals payable from the lease of certain tangible personal property to a qualified person are subject to the partial exemption for a period of six years from the date of inception of the lease. The lease must commence during the time in which this Certificate is valid. *Attach a copy of the lease agreement.

PRINT NAME OF PURCHASER OR PURCHASER'S AUTHORIZED REPRESENTATIVE	TITLE	
SIGNATURE	DATE	PERMIT NUMBER

**** NOT VALID UNLESS COMPLETED BY THE CALIFORNIA STATE BOARD OF EQUALIZATION**

The following business has been registered as a "qualified person" who has certified that this purchase/lease of tangible personal property will be used in a manner entitling them to the exemption provided in Section 6377 of the Revenue and Taxation Code.

BUSINESS NAME	SIC CODE
BUSINESS ADDRESS (Street, City, State, Zip Code)	PERMIT NUMBER

****AUTHORIZED BY: (Must be signed by two Board representatives)**

REVIEWED BY	DATE
APPROVED BY	DATE

**** WHEN COMPLETED AND SIGNED, THIS FORM MAY BE REPRODUCED FOR USE BY THE QUALIFIED PERSON LISTED ABOVE**

Regulation 1525.3. Manufacturing Equipment—Leases of Tangible Personal Property.

(a) ~~General Application to Leases. Leases of tangible personal property which are classified as “continuing sales” and “continuing purchases” of tangible personal property, in accordance with Regulation 1660, “Leases of Tangible Personal Property—In General,” may qualify for the partial exemption from tax for manufacturing equipment, under the conditions set forth in paragraph (i)(1) of Regulation 1525.2, “Manufacturing Equipment.” Lease transactions which qualify for the partial exemption are taxed at the rate specified in Regulation 1525.2, paragraph (a).~~

(b) ~~Recharacterization. With respect to transactions which the parties denominate as a “lease,” but which are recharacterized for sales and use tax purposes either as sales at their inception, pursuant to Regulation 1641, “Credit Sales and Repossessions,” paragraph (b), or as sales under a security agreement, Regulation 1660, “Leases of Tangible Personal Property—In General,” paragraph (a)(2), the transactions may qualify for the partial exemption, in accordance with Regulation 1525.2.~~

(c) ~~Continuation of Partial Exemption. Where possession of tangible personal property is transferred to a qualified person as defined in paragraphs (c) and (d) of Regulation 1525.2 and pursuant to a lease agreement classified as a continuing sale and continuing purchase, lease receipts shall remain partially exempt for a period of six years from the date of the inception of the lease whether or not the lessee remains as a qualified person throughout the six year period. At the close of the six year period from the date of the inception of the lease, lease receipts are subject to tax without exemption.~~

(d) ~~Leases of Tax Paid Property. The partial exemption is not available to lessors who lease to qualified persons or to vendors to such lessors when the lessor elects to pay sales tax reimbursement at the time of acquisition of the property or pays use tax measured by the purchase price of the property.~~

(e) ~~Manufacturers Who Lease Qualified Property. A lease of tangible personal property by the manufacturer of that property is ordinarily regarded as a “continuing sale” and “continuing purchase” in accordance with Regulation 1660, “Leases of Tangible Personal Property—In General.” Nevertheless, beginning January 1, 1997, a lessor of tangible personal property described in sections 17053.49 or 23649 of the Revenue and Taxation Code, who is the manufacturer of that property and who leases that property to a qualified person, as defined in section 17053.49 or 23649 of the Revenue and Taxation Code, in a form that is not substantially the same form as acquired, may, in lieu of reporting tax measured by the rentals payable, elect to pay tax measured by the cost price of that property where the election is made on or before the due date of the return for the period in which the property is first leased to the qualified person. The election shall be made by reporting use tax measured by the cost price of that property on the return for that period. The election shall not be revoked with respect to the property as to which it is made. The lease of that property for which an election is made to report and pay tax on the cost price of that property shall thereafter be excluded from the classification of a “continuing sale” and “continuing purchase.”~~

For purposes of this subdivision, "cost price" means the price at which similar property has been previously sold or offered for sale. If that property has not been previously sold or offered for sale, then the cost price shall be deemed to be the aggregate of the following:

(1) Cost of materials.

(2) Direct labor.

(3) The pro-rata share of all overhead costs attributable to the manufacturer of the property.

(4) Reasonable profit from the manufacturing operations which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the factors listed in subsections (1) to (3), inclusive.

(f) Operative Date. All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or use made after December 31, 2003.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6244.5 and 6377, Revenue and Taxation Code.

Senate Bill No. 38

CHAPTER 954

An act to add Section 17008.7 to, and to add Chapter 3.7 (commencing with Section 50199.50) to Part 1 of Division 31 of, the Health and Safety Code, to amend Sections 6358, 6366, 6377, 17052.12, 17053.8, 17053.49, 17062, 17072, 17076, 17144, 17250, 17271, 17276, 17507, 19144, 19147, 19148, 19191, 19192, 23221, 23609, 23622, 23649, 24307, 24344, 24358, 24411, 24416, 24424, and 24443 of, to amend, repeal, and add Sections 17151, 18042, and 24611 of, to add Sections 6244.5, 17052.8, 17053.12, 17053.14, 17053.42, 17053.73, 17077.5, 17084, 17134.5, 17138.5, 17141.5, 17150, 17201.5, 17210, 17213, 17218, 17255, 17267, 17279.5, 17330, 17570, 17859, 17860, 18044, 23604, 23608, 23608.2, 23608.3, 23622.5, 23642, 23701z, 24343.3, 24344.7, 24472, 24710, 24903, and 24905.5 to, and to add and repeal Sections 17052.10 and 23610 of, the Revenue and Taxation Code, and to amend Section 1088.5 of the Unemployment Insurance Code, relating to taxation, to take effect immediately, tax levy.

[Approved by Governor September 26, 1996 Filed
with Secretary of State September 26, 1996.]

LEGISLATIVE COUNSEL'S DIGEST

SB 38, Lockyer. Taxation.

(1) Existing law authorizes the California Tax Credit Allocation Committee to administer the low-income housing tax credit program.

This bill would enact the Farmworker Housing Assistance Program and would express findings and declarations of the Legislature with respect to the supply of affordable housing for transient and resident farmworkers.

Under the bill, the recipient of a tax credit pursuant to the program or the owner of the assisted farmworker housing would be required to enter into an agreement required by the committee to further the purposes of the program, wherein the owner would agree, among other things, that the farmworker housing units assisted with the farmworker housing tax credits would be utilized, maintained, and operated pursuant to these provisions for the compliance term specified by the applicable farmworker housing tax credit statute. The bill also would restrict the availability, occupancy, and use of the assisted farmworker housing, as specified. By requiring that the agreement be recorded in the official records of the county, this bill would impose a state-mandated local program.

The bill also would require the committee to allocate farmworker housing credits on a regular basis in each calendar year during which

applications may be filed and considered. The committee would be required to establish application procedures, as specified. The bill also would authorize the committee to charge a fee of tax credit applicants as a condition of submitting an application, or receiving an allocation or reservation of tax credits, to defray the committee's costs in administering the program.

(2) The Sales and Use Tax Law imposes a tax on the gross receipts from the sale in this state of, or the storage, use, or other consumption in this state of, tangible personal property and provides various exemptions from the taxes imposed by that law. That law provides an exemption from those taxes for the gross receipts from the sale of, and the storage, use, or other consumption of, tangible personal property, as defined, purchased for use by a qualified person, as defined, primarily in any stage of manufacturing, processing, refining, fabricating, or recycling of property, and introduced into the process, as specified. That law also provides that if a purchaser who gives a resale certificate or purchases property for the purpose of reselling it makes any storage or use of the property, except as provided, the storage and use is taxable, and, with respect to specified property for which the use is limited to leasing, the purchaser is allowed to pay the use tax measured by the fair rental value, as defined.

This bill would provide under that law that a lessor of property that is the subject of that exemption, who is a manufacturer of that property, and who leases that property in a specified form, may, in lieu of reporting use tax measured by the rentals payable, elect to pay tax measured by his or her cost price, as defined, of that property if the election is made, as provided.

(3) The Sales and Use Tax Law also provides an exemption for drugs or medicines administered to animal life as an additive to feed or drinking water, the primary purpose of which is the prevention and control of disease of food animals, or of nonfood animals which are to be sold in the regular course of business.

This bill would additionally provide an exemption from those taxes for drugs or medicines, the primary purpose of which is the prevention or control of disease, that are administered to animal life of a kind the products of which ordinarily constitute food for human consumption.

(4) The Sales and Use Tax Law also provides an exemption for aircraft used as a common carrier, as specified, or sold to any person who is not a resident of this state and who will not use the aircraft in this state.

This bill would additionally exempt tangible personal property purchased on or after October 1, 1996, that becomes a component part of those aircraft as a result of the maintenance, repair, overhaul, or improvement of an aircraft, in compliance with federal requirements, and any charges made for labor and services rendered with respect thereto, as provided.



* (5) The Sales and Use Tax Law also provides an exemption for tangible personal property, as defined, purchased for use by a qualified person, as defined, primarily in any stage of manufacturing, processing, refining, fabricating, or recycling of property, and introduced into the process, as specified.

The Personal Income Tax Law and the Bank and Corporation Tax Law allow to qualified taxpayers, as defined, a credit against taxes imposed by those laws in an amount equal to 6% of the amount paid or incurred during the taxable or income year for qualified property, as defined, that is placed in service in this state. Existing law provides that qualified property includes tangible personal property for use by a qualified taxpayer, as defined, primarily for the manufacturing, processing, refining, fabricating, or recycling of property, and introduced into the process, as specified.

This bill would define the term "process" for purposes of those provisions of sales and use taxes, personal income taxes, and bank and corporation taxes relating to the introduction of property into the process, and would apply the above sales and use tax exemption to leases of tangible personal property, as specified.

This bill would also expand the definition of qualified property under the Personal Income Tax Law and the Bank and Corporation Tax Law to include specified property related to certain activities in connection with space vehicles, parts, and satellites or semiconductor manufacturing equipment, as specified. The bill would require that, in the case of any partnership or S corporation, the qualification for the credit shall be determined at the entity level, and the credit passed through to the partner or shareholder. The bill would also authorize the Franchise Tax Board to issue specified regulations in connection with the credit.

The Personal Income Tax Law and the Bank and Corporation Tax Law permit any qualified taxpayer to carry over any unused portion of the above credit for the following 8 taxable or income years and permits any small business, as defined, to carry over any unused portion of that credit for the following 10 taxable or income years.

This bill would include any qualified taxpayer engaged in biopharmaceutical activities, as defined, or engaged in biotechnology activities, as defined, that has not received federal regulatory approval for any product, as specified, within the definition of "small business," thereby allowing those qualified taxpayers a longer carryover period for the credit.

(6) The Personal Income Tax Law and the Bank and Corporation Tax Law authorize a specified net operating loss deduction against the taxes imposed by those laws, including provisions that permit those losses to be carried forward 5 taxable or income years, as specified, or in the case of a new business, as defined, for an additional one to 3 taxable or income years, as specified.



(1) Aircraft sold to any person using the aircraft as a common carrier of persons or property under authority of the laws of this state, of the United States, or of any foreign government, or sold to any foreign government for use by that government outside of this state, or sold to any person who is not a resident of this state and who will not use that aircraft in this state otherwise than in the removal of the aircraft from this state.

(2) Tangible personal property that is purchased on or after October 1, 1996, and becomes a component part of any aircraft described in paragraph (1), as a result of the maintenance, repair, overhaul, or improvement of that aircraft in compliance with Federal Aviation Administration requirements, and any charges made for labor and services rendered with respect to that maintenance, repair, overhaul, or improvement.

(b) With respect to aircraft sold on or after January 1, 1997, it shall be presumed that a person is not engaged in business as a common carrier if the person's yearly gross receipts from the use of the aircraft as a common carrier do not exceed 20 percent of the purchase cost of the aircraft to him or her, or fifty thousand dollars (\$50,000), whichever is less. This presumption may be rebutted by contrary evidence satisfactory to the board showing that the person is engaged in business as a common carrier.

In no event shall "gross receipts" include compensation by the person or related parties for use of the aircraft as a common carrier.

(c) With respect to aircraft leased, or sold for the purpose of leasing, on or after January 1, 1997, it shall be presumed that the aircraft is not regularly used in the business of transporting for hire property or persons if the lessor's yearly gross receipts from the lease of that aircraft to persons using the aircraft as common carriers of property or persons do not exceed 20 percent of the cost of the aircraft to the lessor, or fifty thousand dollars (\$50,000), whichever is less. This presumption may be rebutted by contrary evidence satisfactory to the board showing that the aircraft is regularly used as a common carrier of property or persons.

In no event shall "gross receipts" include compensation by the lessor or related parties for use of the aircraft as a common carrier.

SEC. 6. Section 6377 of the Revenue and Taxation Code is amended to read:

* 6377. (a) There are exempted from the taxes imposed by this part the gross receipts from the sale of, and the storage, use, or other consumption in this state of, any of the following:

(1) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point any raw materials are received by the qualified person and introduced into the process and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling has



altered property to its completed form, including packaging, if required.

(2) Tangible personal property purchased for use by a qualified person to be used primarily in research and development.

(3) Tangible personal property purchased for use by a qualified person to be used primarily to maintain, repair, measure, or test any property described in paragraph (1) or (2).

(4) Tangible personal property purchased for use by a contractor purchasing that property either as an agent of a qualified person or for the contractor's own account and subsequent resale to a qualified person for use in the performance of a construction contract for the qualified person who will use the tangible personal property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, or as a research or storage facility for use in connection with the manufacturing process.

This exemption shall not apply to any tangible personal property that is used primarily in administration, general management, or marketing.

(b) For purposes of this section:

(1) "Fabricating" means to make, build, create, produce, or assemble components or property to work in a new or different manner.

(2) "Manufacturing" means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property.

(3) "Primarily" means tangible personal property used 50 percent or more of the time in an activity described in subdivision (a).

(4) "Process" means the period beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer has altered tangible personal property to its completed form, including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified taxpayer's manufacturing, processing, refining, or recycling activity is conducted. Raw materials that are stored on premises other than where the qualified taxpayer's manufacturing, processing, refining, fabricating, or recycling activity is conducted, shall not be considered to have been introduced into the manufacturing, processing, refining, fabricating, or recycling process.



(5) "Processing" means the physical application of the materials and labor necessary to modify or change the characteristics of property.

(6) "Qualified person" means any person that is both of the following:

(A) A new trade or business. In determining whether a trade or business activity qualifies as a new trade or business, the following rules shall apply:

(i) In any case where a person purchases or otherwise acquires all or any portion of the assets of an existing trade or business (irrespective of the form of entity) that is doing business in this state (within the meaning of Section 23101), the trade or business thereafter conducted by that person (or any related person) shall not be treated as a new business if the aggregate fair market value of the acquired assets (including, real, personal, tangible, and intangible property) used by that person (or any related person) in the conduct of his or her trade or business exceed 20 percent of the aggregate fair market value of the total assets of the trade or business being conducted by the person (or any related person). For purposes of this subparagraph only, the following rules shall apply:

(I) The determination of the relative fair market values of the acquired assets and the total assets shall be made as of the last day of the month following the quarterly period in which the person (or any related person) first uses any of the acquired trade or business assets in his or her business activity.

(II) Any acquired assets that constituted property described in Section 1221(1) of the Internal Revenue Code in the hands of the transferor shall not be treated as assets acquired from an existing trade or business, unless those assets also constitute property described in Section 1221(1) of the Internal Revenue Code in the hands of the acquiring person (or related person).

(ii) In any case where a person (or any related person) is engaged in one or more trade or business activities in this state, or has been engaged in one or more trade or business activities in this state within the preceding 36 months ("prior trade or business activity"), and thereafter commences an additional trade or business activity in this state, the additional trade or business activity shall only be treated as a new business if the additional trade or business activity is classified under a different division of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition, than are any of the person's (or any related person's) current or prior trade or business activities in this state.

(iii) In any case where a person, including all related persons, is engaged in trade or business activities wholly outside of this state and that person first commences doing business in this state (within the meaning of Section 23101) after December 31, 1993 (other than by



purchase or other acquisition described in clause (i)), the trade or business activity shall be treated as a new business.

(iv) In any case where the legal form under which a trade or business activity is being conducted is changed, the change in form shall be disregarded and the determination of whether the trade or business activity is a new business shall be made by treating the person as having purchased or otherwise acquired all or any portion of the assets of an existing trade or business under the rules of clause (i).

(v) "Related person" means any person that is related to that person under either Section 267 or 318 of the Internal Revenue Code.

(vi) "Acquire" includes any gift, inheritance, transfer incident to divorce, or any other transfer, whether or not for consideration.

(B) Engaged in those lines of business described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition.

(7) Notwithstanding paragraph (6), "qualified person" shall not include any person who has conducted business activities in a new trade or business for three or more years.

(8) "Refining" means the process of converting a natural resource to an intermediate or finished product.

(9) "Research and development" means those activities that are described in Section 174 of the Internal Revenue Code or in any regulations thereunder.

(10) "Tangible personal property" does not include any of the following:

(A) Consumables with a normal useful life of less than one year, except as provided in subparagraph (E) of paragraph (10).

(B) Furniture, inventory, equipment used in the extraction process, or equipment used to store finished products that have completed the manufacturing process.

(C) Any property for which a credit is claimed under either Section 17053.49 or 23649.

(11) "Tangible personal property" includes, but is not limited to, all of the following:

(A) Machinery and equipment, including component parts and contrivances such as belts, shafts, moving parts, and operating structures.

(B) All equipment or devices used or required to operate, control, regulate, or maintain the machinery, including, without limitation, computers, data processing equipment, and computer software, together with all repair and replacement parts with a useful life of one or more years therefor, whether purchased separately or in conjunction with a complete machine and regardless of whether the machine or component parts are assembled by the taxpayer or another party.

(C) Property used in pollution control that meets or exceeds standards established by this state or any local or regional governmental agency within this state.

(D) Special purpose buildings and foundations used as an integral part of the manufacturing, processing, refining, or fabricating process, or that constitute a research or storage facility used during the manufacturing process. Buildings used solely for warehousing purposes after completion of the manufacturing process are not included.

(E) Fuels used or consumed in the manufacturing process.

(F) Property used in recycling.

(c) No exemption shall be allowed under this section unless the purchaser furnishes the retailer with an exemption certificate, completed in accordance with any instructions or regulations as the board may prescribe, and the retailer subsequently furnishes the board with a copy of the exemption certificate. The exemption certificate shall contain the sales price of the machinery or equipment that is exempt pursuant to subdivision (a).

(d) Notwithstanding any provision of the Bradley-Burns Uniform Local Sales and Use Tax Law (Part 1.5 (commencing with Section 7200)) or the Transactions and Use Tax Law (Part 1.6 (commencing with Section 7251)), the exemption established by this section shall not apply with respect to any tax levied by a county, city, or district pursuant to, or in accordance with, either of those laws.

(e) (1) Notwithstanding subdivision (a), the exemption provided by this section shall not apply to any sale or use of property which, within one year from the date of purchase, is either removed from California or converted from an exempt use under subdivision (a) to some other use not qualifying for the exemption.

(2) Notwithstanding subdivision (a), on or after January 1, 1995, the exemption established by this section shall not apply with respect to any tax levied pursuant to Sections 6051.2 and 6201.2, or pursuant to Section 35 of Article XIII of the California Constitution.

(f) If a purchaser certifies in writing to the seller that the property purchased without payment of the tax will be used in a manner entitling the seller to regard the gross receipts from the sale as exempt from the sales tax, and within one year from the date of purchase, the purchaser (1) removes that property outside California, (2) converts that property for use in a manner not qualifying for the exemption, or (3) uses that property in a manner not qualifying for the exemption, the purchaser shall be liable for payment of sales tax, with applicable interest, as if the purchaser were a retailer making a retail sale of the property at the time the property is so removed, converted, or used, and the sales price of the property to the purchaser shall be deemed the gross receipts from that retail sale.

(g) (1) This section shall remain in effect until the date specified in paragraph (2), on which date this section shall cease to be operative, and as of that date is repealed.

(2) (A) This section shall cease to be operative on January 1, 2001, or on January 1 of the earliest year thereafter, if the total employment in this state, as determined by the Employment Development Department on the preceding January 1, does not exceed by 100,000 jobs the total employment in this state on January 1, 1994. The department shall report annually to the Legislature with respect to the determination required by the preceding sentence.

(B) For purposes of this paragraph, "total employment" means the total employment in the manufacturing sector, excluding employment in the aerospace sector.

(h) This section applies to leases of tangible personal property classified as "continuing sales" and "continuing purchases" in accordance with Sections 6006.1 and 6010.1. The exemption established by this section shall apply to the rentals payable pursuant to such a lease, provided the lessee is a qualified person and the property is used in an activity described in subdivision (a). Rentals which meet the foregoing requirements are eligible for the exemption for a period of six years from the date of commencement of the lease. At the close of the six-year period from the date of commencement of the lease, lease receipts are subject to tax without exemption.

SEC. 6.1. Section 17052.8 is added to the Revenue and Taxation Code, to read:

17052.8. For each taxable year beginning on or after January 1, 1996, there shall be allowed as a credit against the "net tax" (as defined by Section 17039) an amount determined as follows:

(a) (1) (A) The amount of the credit shall be equal to one-third of the federal credit computed in accordance with Section 43 of the Internal Revenue Code.

(B) If a taxpayer elects, under Section 43(e) of the Internal Revenue Code, not to apply Section 43 for federal tax purposes, this election is binding and irrevocable for state purposes, and for purposes of subparagraph (A), the federal credit shall be zero.

(2) "Qualified enhanced oil recovery project" shall include only projects located within California.

(3) The credit allowed under this subdivision shall not be allowed to any taxpayer for whom a depletion allowance is not permitted to be computed under Section 613 of the Internal Revenue Code by reason of paragraphs (2), (3), or (4) of subsection (d) of Section 613A of the Internal Revenue Code.

(b) Section 43(d) of the Internal Revenue Code shall apply.

(c) In the case where the credit allowed by this section exceeds the "net tax," the excess may be carried over to reduce the "net tax" for the succeeding 15 years.



Memorandum

To : Ms. Cynthia Bridges
Executive Director, MIC:73

Date: April 3, 2014

From : Randy Ferris, Chief Counsel ^{RMF}
Legal Department, MIC:83

Subject : Board Meeting, April 22-23, 2014
Item J - Chief Counsel's Rulemaking Calendar
Regulation 1525.2, Manufacturing Equipment
Regulation 1525.3, Manufacturing Equipment – Leases of Tangible Personal Property

We request your approval to place the proposed repeal of Sales and Use Tax Regulations 1525.2, *Manufacturing Equipment*, and 1525.3, *Manufacturing Equipment – Leases of Tangible Personal Property*, on the Chief Counsel's Rulemaking Calendar for the April 22-23, 2014, Board meeting. Regulation 1525.2 implements, interprets, and makes specific the provisions of Revenue and Taxation Code section (section) 6377. Regulation 1525.3 further prescribes the application of section 6377 to lease transactions. Section 6377 was added by Statutes 1993, chapter 881 (Sen. Bill No. 671) and provided a partial exemption from sales and use tax for certain property purchased by a qualified person to be used primarily in specified activities, including manufacturing, as described in the regulations, until it was repealed by its own terms, effective January 1, 2004.

We will request the Board's authorization to repeal Regulations 1525.2 and 1525.3 under California Code of Regulations, title 1, section (Rule) 100, without the normal notice and public hearing process. The repeal of the regulations is appropriate for processing under Rule 100 because the statutory basis for the regulations, section 6377, has been repealed.

Attached are strikeout versions of Regulations 1525.2 and 1525.3 illustrating the repeal of the regulations, including appendices A and B to Regulation 1525.2.

If you have any questions regarding this request, please let me know or contact Mr. Bradley Heller at 323-3091.

Recommendation by:

Approved:


Randy Ferris, Chief Counsel


Cynthia Bridges, Executive Director

STATE BOARD OF EQUALIZATION



BOARD APPROVED

At the April 22, 2014 Board Meeting

Item J1
04/22/14


Joann Richmond, Chief
Board Proceedings Division

Regulation 1525.2 MANUFACTURING EQUIPMENT

Reference: Section 6377, Revenue and Taxation Code.

~~(a) PARTIAL EXEMPTION FOR PROPERTY PURCHASED FOR USE IN THE MANUFACTURING PROCESS.~~

~~Section 6377 of the Revenue and Taxation Code provides a partial exemption from sales and use tax for certain properties described in this regulation.~~

~~For the period commencing on January 1, 1994, and ending on December 31, 1994, the partial exemption applies to the taxes imposed by the state (6%), but does not apply to the taxes imposed by counties, cities, and districts pursuant to the Bradley Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code §§ 7200, et seq.) or the Transactions and Use Tax Law (Rev. & Tax. Code §§ 7251, et seq.).~~

~~For the period commencing on January 1, 1995, and ending on December 31, 2000, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2001, and ending on December 31, 2001, the partial exemption applies to the taxes imposed by sections 6051 and 6201 of the Revenue and Taxation Code (4.75%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~For the period commencing on January 1, 2002, and ending on December 31, 2003, the partial exemption applies to the taxes imposed by sections 6051, 6051.3, 6201, and 6201.3 of the Revenue and Taxation Code (5%), but does not apply to the taxes imposed pursuant to sections 6051.2 and 6201.2 of the Revenue and Taxation Code, the Bradley Burns Uniform Local Sales and Use Tax Law, the Transactions and Use Tax Law, or section 35 of article XIII of the California Constitution.~~

~~Pursuant to the provisions of the Revenue and Taxation Code section 6377(g), the partial exemption from tax on the sale and use of property used in manufacturing and related activities as described in this regulation expired on December 31, 2003.~~

~~Subject to the limitations set forth above, this partial exemption applies to gross receipts from the sale, storage, use, or other consumption in this state of the following items:~~

~~— (1) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point that raw materials are received by the qualified person and introduced into the process and ending at the point at which the property has been altered to its completed form, including packaging, if required. For purposes of this regulation:~~

~~— (A) Raw materials will be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified person's manufacturing activities are conducted. Raw materials that are stored on premises other than where the qualified person's manufacturing activities are conducted, however, will not be considered to have been introduced into the process for purposes of this regulation.~~

~~— (B) For purposes of this regulation, the term "packaging" includes only that packaging necessary to prepare the goods for delivery to and placement in the qualified person's finished goods inventory, or to prepare the goods so that they are suitable for delivery to and placement in finished goods inventory. Any additional packaging, such as that packaging necessary to consolidate the goods prior to shipping or to protect them during transportation, shall not be considered to be "packaging" for purposes of this regulation.~~

~~— (2) Tangible personal property purchased for use by a qualified person to be used primarily in research and development as defined in subdivision (c)(8).~~

~~— (3) Tangible personal property purchased for use by a qualified person to be used primarily to maintain, repair, measure, or test any property described in subdivision (a)(1) or (a)(2).~~

Regulation 1525.2 (Continued)

business activities. In determining whether or not a person is qualified within the meaning of this subdivision, the following rules apply:

1. The term "trade or business activities" does not mean the mere formation or organization of a corporation or other business entity that is intended to conduct a trade or business. Instead, a corporation or business entity first conducts activities when it first starts or commences the trade or business for which it was organized. The acquisition of operating assets that are necessary to the type of business contemplated, however, will constitute commencing activities. The term "operating assets" as used in this subdivision means assets that are in a state of readiness to be placed in service within a reasonable time period following their acquisition.

2. Notwithstanding any other provision of this subdivision, a person will not be considered to have first commenced activities in a new trade or business in this state on or after January 1, 1994, if, at any time within the 36 months preceding that date, that person, or any related person, was required to have secured a seller's permit under section 6066 of the Revenue and Taxation Code for that trade or business, or any other trade or business classified under the same division of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition (the "Manual"). For purposes of this regulation, the term "division" means a division as that term is used in the Manual.

3. A trade or business is not a new trade or business in this state if, within the 36 months preceding the date that activities were first commenced in that trade or business in this state, either the person claiming the partial exemption, or any related person, had conducted any activities in this state in any trade or business classified under the same division of the Manual as that trade or business.

4. Where a person, or any related person, is engaged in one or more trade or business activities in this state, or has been engaged in one or more trade or business activities in this state within the preceding 36 months (a "prior trade or business activity"), and thereafter commences an additional trade or business activity in this state, the additional trade or business activity shall only be treated as a new trade or business if the additional trade or business activity is classified under a different division of the Manual than are any of the person's (or any related person's) current or prior trade or business activities in this state within the preceding 36 months.

5. Where a person, including all related persons, is engaged in trade or business activities wholly outside of this state and that person first commences doing business in this state (within the meaning of section 23101 of the Revenue and Taxation Code) after December 31, 1993 (other than by purchase or other acquisition described in subdivision (c)(6)(A)6.), the newly commenced trade or business activity in this state shall be treated as a new trade or business for purposes of this subdivision.

6. On or after January 1, 1995, notwithstanding anything else set forth in this subdivision, in any case where a person purchases or otherwise acquires all or any portion of the assets of an existing trade or business (irrespective of the form of the entity) that is doing business in this state (within the meaning of section 23101 of the Revenue and Taxation Code), the trade or business thereafter conducted by that person (or any related person) shall not be treated as a new trade or business if the aggregate fair market value of the acquired assets (including real, personal, tangible, and intangible property) used by that person (or any related person) in the conduct of his or her trade or business exceeds 20 percent of the aggregate fair market value of the total assets of the person (or any related person) being used in the same trade or business both within and without this state. For purposes of this subdivision only:

a. The determination of the relative fair market values of the acquired assets and the total assets shall be made as of the last day of the month following the quarterly period in which the person (or any related person) first uses any of the acquired trade or business assets in his or her business activity.

b. Any acquired assets that constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the transferor shall not be treated as assets acquired from an existing trade or business, unless those assets also constitute property described in section 1221(a)(1) of the Internal Revenue Code in the hands of the acquiring person (or any related person).

c. The trade or business conducted in this state by the acquiring person after the asset acquisition date shall be considered to be the same as an out-of-state trade or business conducted or previously

Regulation 1525.2 (Continued)

~~1. For purposes of classifying a line or lines of business, the economic unit shall be the "establishment" and the classification of the line or lines of business will be based on the establishment's single most predominant activity based upon value of production. The term "establishment" means an economic unit, generally at a single physical location, where business is conducted or where services or manufacturing or other industrial operations are performed. The following will generally constitute an "establishment": a factory, mill, store, hotel, movie theater, mine, farm, ranch, bank, railroad depot, airline terminal, sales office, warehouse, or central administrative office.~~

~~2. For purposes of determining the "establishment" or "establishments" of a trade or business:~~

~~a. Where distinct and separate economic activities are performed at a single physical location, such as construction activities operated out of the same physical location as a lumber yard, each activity should be treated as a separate establishment where: (i) no one industry description in the classification includes such combined activities; (ii) the employment in each such economic activity is significant; and (iii) separate reports are prepared on the number of employees, their wages and salaries, sales or receipts, property and equipment, and other types of financial data, such as financial statements, job costing, and profit center accounting. For purposes of this paragraph, whether or not employment in an economic activity is significant shall be based upon all of the facts and circumstances. Nevertheless, employment in an economic activity will be considered to be "significant" for purposes of this paragraph whenever more than 25 percent of the taxpayer's total number of employees at a single physical location, or more than 25 percent of the taxpayer's total dollar value of payroll at a single physical location, is attributable to the economic activity being tested for separate establishment status.~~

~~b. An establishment is not necessarily identical with the enterprise or company which may consist of one or more establishments. Also, an establishment is to be distinguished from subunits of the establishment such as departments.~~

~~c. Where a person conducts business at more than one establishment within the meaning of this subdivision, then that person shall be considered to be a "qualified person" for purposes of this regulation only as to those purchases that are intended to be used and are actually used in those lines of business that are described in Codes 2011 to 3999, inclusive, of the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition.~~

~~(7) "Refining" means the process of converting a natural resource to an intermediate or finished product.~~

~~(8) "Research and development" means those activities that are described in section 174 of the Internal Revenue Code or in any regulations thereunder.~~

~~(9) "Tangible personal property" does not include any of the following:~~

~~(A) Real property, including tangible personal property to be incorporated into an improvement to real property, except for "special purpose buildings and foundations" as defined in subdivision (c)(10)(D) and conveyance systems and assembly lines as provided in subdivision (c)(10)(A).~~

~~(B) Consumables with a normal useful life of less than one year, except as provided in subdivision (c)(10)(E). For purposes of this regulation, it shall be presumed tangible personal property that the qualified person treats as having a normal useful life of less than one year for state income or franchise tax purposes is tangible personal property with a normal useful life of less than one year. This presumption may be rebutted by evidence satisfactory to the Board.~~

~~(C) Furniture, inventory, equipment used in the extraction process, equipment used to store raw materials that have not yet entered or commenced the manufacturing process, or equipment used to store finished products that have completed the manufacturing process. The extraction process includes such severance activities as mining, oil and gas extraction.~~

~~(D) Any property for which a credit is claimed under either section 17053.49 or 23649 of the Revenue and Taxation Code.~~

~~(10) "Tangible personal property" includes but is not limited to the following:~~

Regulation 1525.2 (Continued)

~~_____ (F) Property used in recycling.~~

~~_____ (11) "Standard Industrial Classification" means a Standard Industrial Classification in the Standard Industrial Classification Manual published by the United States Office of Management and Budget, 1987 edition.~~

~~(d) **THREE YEAR LIMITATION.** Notwithstanding any other provision of this regulation, once a person has conducted business activities in a new trade or business for three or more years, that person will no longer be considered to be in a "new trade or business," nor "qualified" for this partial exemption.~~

~~(e) **TAXES AS TO WHICH THE PARTIAL EXEMPTION DOES NOT APPLY.** This partial exemption does not apply to any tax levied by a county, city, or district pursuant to, or in accordance with, either the Bradley-Burns Uniform Local Sales and Use Tax Law (Rev. & Tax. Code §§ 7200 et seq.) or the Transactions and Use Tax Law (Rev. & Tax Code §§ 7251 et seq.).~~

~~On or after January 1, 1995, this partial exemption shall not apply to any tax levied pursuant to section 6051.2 and 6201.2 of the Revenue and Taxation Code, or pursuant to section 35 of article XIII of the California Constitution.~~

~~(f) **EXEMPTION CERTIFICATES.** Except as otherwise set forth in subdivision (f)(3), to claim the partial exemption provided by this regulation, a person must be both pre-qualified by the Board and either registered to hold a seller's permit or maintain a consumer use tax account. Exemption certificates issued to qualified persons will contain a control number and expiration date for verifying a person's status as a qualified person. An exemption certificate is not valid if it has not been issued by the Board or if it is accepted after the expiration date on the certificate. Qualified persons who have been pre-qualified may reproduce the issued certificates as needed for their qualifying purchases.~~

~~The exemption certificates issued by the Board will be in substantially the same form as they appear in Appendices A and B of this regulation. Qualified persons who purchase or lease tangible personal property from an in-state retailer or an out-of-state retailer obligated to collect the use tax must provide the retailer with a manufacturer's exemption certificate in order to claim the partial exemption. The manufacturer's use tax declaration must be completed by a qualified person to claim a partial exemption from use tax on purchases of tangible personal property from an out-of-state retailer not obligated to collect the use tax.~~

~~Solely for the purposes of this regulation, it is presumed that a seller accepts a manufacturer's exemption certificate from a prequalified purchaser in good faith in the absence of evidence to the contrary. A retailer's direct knowledge that the purchaser is not purchasing tangible personal property for use in a manufacturing activity, that the purchaser intends the tangible personal property for his or her own use, or that the tangible personal property does not have a normal useful life of one year or more constitutes evidence to the contrary. A purchaser providing a manufacturer's exemption certificate accepted in good faith by the seller for tangible personal property that does not qualify for this exemption is liable for the payment of tax as set forth in subdivision (h).~~

~~_____ (1) **MANUFACTURER'S EXEMPTION CERTIFICATES.**~~

~~_____ (A) **In General.** Except as otherwise provided in subdivisions (f)(1)(B) or (f)(3) of this regulation, or in section 6902.2 of the Revenue and Taxation Code, a partial exemption from sales or use tax shall not be allowed unless:~~

~~_____ 1. The qualified person furnishes the retailer with a manufacturer's exemption certificate no later than 60 days after the date of the purchase; and~~

~~_____ 2. The retailer timely files a sales and use tax return claiming the partial exemption and, together with that timely return, provides the Board with a copy of the manufacturer's exemption certificate.~~

~~_____ (B) **Exclusions.** Except as provided in subdivision (f)(1)(C) below, retailers claiming the partial exemption in timely filed returns will not be required to furnish the Board with copies of manufacturer's exemption certificates for sales or leases of tangible personal property made by a retailer at any single physical location to a single qualified purchaser that do not exceed an aggregate total of \$25,000 during a single calendar quarter. Regardless of the total quarterly sales per purchaser, however, when necessary for the efficient administration of the sales and use tax law, the Board may, on 30 days' written notice, require a retailer to commence furnishing the Board with copies of all certificates on a quarterly basis pursuant to subdivision (f)(1)(A)2.~~

Regulation 1525.2 (Continued)

~~(h) PURCHASER'S LIABILITY FOR THE PAYMENT OF SALES TAX.~~ If a purchaser submits a copy of a manufacturer's exemption certificate to the seller, and then within one year from the later of the date of purchase of the property or the date that the property was first placed into service by the purchaser in an exempt use, the purchaser either (i) removes that property from this state, (ii) converts that property from an exempt use under this regulation to some other use not qualifying for the partial exemption, or (iii) uses that property in a manner not qualifying for the partial exemption under this regulation, then, in that event, the purchaser shall be liable for payment of sales tax, with applicable interest, to the same extent as if the purchaser were a retailer making a retail sale of the property at the time the property was so removed, converted, or used; and the sales price of the property to the purchaser shall be deemed to be the gross receipts from that retail sale. For purposes of this subdivision, property is converted to a use not qualifying for the partial exemption if, without limitation, the property, or any interest in the property, or possession or control of the property, is either directly or indirectly sold, transferred, leased, or assigned to a person who is not a qualified person on the date the property is sold, transferred, leased, or assigned to such nonqualified person.

~~(i) LEASES TO QUALIFYING PERSONS.~~

~~— (1) LEASES IN GENERAL.~~ Subject to all the limitations and conditions set forth in this regulation and regulation 1525.3, this partial exemption may apply to rental receipts paid by a qualified person with respect to a lease of tangible personal property to the qualified person, which tangible personal property is used as set forth in subdivisions (a)(1), (a)(2), (a)(3), or (a)(4) of this regulation.

~~— (2) LEASES ACQUISITION SALE AND LEASEBACK.~~ A person will be regarded as having paid sales tax reimbursement or use tax with respect to that person's purchase of property, within the meaning of those words as they are used in section 6010.65 of the Revenue and Taxation Code, if the person has paid all applicable taxes with respect to the acquisition of the property, notwithstanding the fact that the sale and purchase of the property may have been subject to the partial exemption from tax provided by this regulation.

~~— (3) SUBSEQUENT LEASE OF PROPERTY ACQUIRED SUBJECT TO PARTIAL EXEMPTION.~~ If a person has acquired property subject to the partial exemption provided by this regulation and has paid all applicable taxes at that acquisition, the property will be regarded as property as to which sales tax reimbursement or use tax has been paid, and the subsequent lease of that property will not be subject to tax measured by rental receipts.

~~(j) OPERATIVE DATE.~~ Except as expressly set forth otherwise in subdivisions (c)(6)(A)6. and (e) of this regulation, this regulation is operative as of January 1, 1994. All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for a sale or a use made after December 31, 2003.

SECTION 6377 MANUFACTURER'S USE TAX DECLARATION

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

PLEASE NOTE

This is a partial exemption from sales and use taxes at the rate of 5% effective January 1, 2002, 4.75% from January 1, 2001 to December 31, 2001, and 5% from January 1, 1996 to December 31, 2000. You are not relieved from your obligations for the local and district taxes on this transaction. The exemption is specific to this transaction only and may not be construed to exempt other transactions. Generally, the partial exemption will not be allowed unless this certificate is issued within 60 days after the date of purchase and the retailer claims the exemption on a timely filed return. Void after expiration date. Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer's Exemption Certificates for sales made after December 31, 2003. Questions regarding this certificate should be directed to: [insert contact information]

Certificate No:
Valid Period Begins:
Valid Period Expires:
(*See below for leases)

I hereby certify that the tangible personal property described below that is subject to use tax was purchased or is being leased from:
(enter seller's/lessor's name and address)

SELLER'S NAME

SELLER'S ADDRESS (Street, City, State, Zip Code)

and will be used by me primarily (please check one)

- 1. for manufacturing, processing, refining, fabricating, or recycling, or
- 2. for research and development activities as described in Internal Revenue Code Section 174, or
- 3. to maintain, repair, measure, or test any property being used for (1) or (2) above, at my facility located at (enter facility's address):

(Street, City, State, Zip Code)

SALES INVOICE NUMBER	SALES INVOICE DATE	DESCRIPTION OF PROPERTY PURCHASED OR LEASED*	SALES PRICE/ RENTALS PAYABLE

I understand that if such property is, within one year from the date of purchase or lease, removed from California or converted for use or otherwise used in a manner not qualifying for the partial exemption that I am required by the Sales and Use Tax Law to report and pay the state tax measured by the sales price/rentals payable of the property to/by me. Taxable rentals payable from the lease of certain tangible personal property to a qualified person are subject to the partial exemption for a period of six years from the date of inception of the lease. The lease must commence during the time in which this Certificate is valid. *Attach a copy of the lease agreement.

PRINT NAME OF PURCHASER OR PURCHASER'S AUTHORIZED REPRESENTATIVE	TITLE
SIGNATURE	DATE
PERMIT NUMBER	

**** NOT VALID UNLESS COMPLETED BY THE CALIFORNIA STATE BOARD OF EQUALIZATION**

The following business has been registered as a "qualified person" who has certified that this purchase/lease of tangible personal property will be used in a manner entitling them to the exemption provided in Section 6377 of the Revenue and Taxation Code.

BUSINESS NAME	SIC CODE
BUSINESS ADDRESS (Street, City, State, Zip Code)	PERMIT NUMBER

****AUTHORIZED BY: (Must be signed by two Board representatives)**

REVIEWED BY	DATE
APPROVED BY	DATE

** WHEN COMPLETED AND SIGNED, THIS FORM MAY BE REPRODUCED FOR USE BY THE QUALIFIED PERSON LISTED ABOVE

Regulation 1525.3. ~~MANUFACTURING EQUIPMENT—LEASES OF TANGIBLE PERSONAL PROPERTY.~~

Reference: Sections 6244.5 and 6377, Revenue and Taxation Code.

~~(a) GENERAL APPLICATION TO LEASES.~~ Leases of tangible personal property which are classified as “continuing sales” and “continuing purchases” of tangible personal property, in accordance with Regulation 1660, “Leases of Tangible Personal Property In General,” may qualify for the partial exemption from tax for manufacturing equipment, under the conditions set forth in paragraph (i)(1) of Regulation 1525.2, “Manufacturing Equipment.” Lease transactions which qualify for the partial exemption are taxed at the rate specified in Regulation 1525.2, paragraph (a).

~~(b) RECHARACTERIZATION.~~ With respect to transactions which the parties denominate as a “lease,” but which are recharacterized for sales and use tax purposes either as sales at their inception, pursuant to Regulation 1641, “Credit Sales and Repossessions,” paragraph (b), or as sales under a security agreement, Regulation 1660, “Leases of Tangible Personal Property In General,” paragraph (a)(2), the transactions may qualify for the partial exemption, in accordance with Regulation 1525.2.

~~(c) CONTINUATION OF PARTIAL EXEMPTION.~~ Where possession of tangible personal property is transferred to a qualified person as defined in paragraphs (c) and (d) of Regulation 1525.2 and pursuant to a lease agreement classified as a continuing sale and continuing purchase, lease receipts shall remain partially exempt for a period of six years from the date of the inception of the lease whether or not the lessee remains as a qualified person throughout the six year period. At the close of the six year period from the date of the inception of the lease, lease receipts are subject to tax without exemption.

~~(d) LEASES OF TAX PAID PROPERTY.~~ The partial exemption is not available to lessors who lease to qualified persons or to vendors to such lessors when the lessor elects to pay sales tax reimbursement at the time of acquisition of the property or pays use tax measured by the purchase price of the property.

~~(e) MANUFACTURERS WHO LEASE QUALIFIED PROPERTY.~~ A lease of tangible personal property by the manufacturer of that property is ordinarily regarded as a “continuing sale” and “continuing purchase” in accordance with Regulation 1660, “Leases of Tangible Personal Property In General.” Nevertheless, beginning January 1, 1997, a lessor of tangible personal property described in sections 17053.49 or 23649 of the Revenue and Taxation Code, who is the manufacturer of that property and who leases that property to a qualified person, as defined in section 17053.49 or 23649 of the Revenue and Taxation Code, in a form that is not substantially the same form as acquired, may, in lieu of reporting tax measured by the rentals payable, elect to pay tax measured by the cost price of that property where the election is made on or before the due date of the return for the period in which the property is first leased to the qualified person. The election shall be made by reporting use tax measured by the cost price of that property on the return for that period. The election shall not be revoked with respect to the property as to which it is made. The lease of that property for which an election is made to report and pay tax on the cost price of that property shall thereafter be excluded from the classification of a “continuing sale” and “continuing purchase.”

For purposes of this subdivision, “cost price” means the price at which similar property has been previously sold or offered for sale. If that property has not been previously sold or offered for sale, then the cost price shall be deemed to be the aggregate of the following:

- (1) Cost of materials.
- (2) Direct labor.
- (3) The pro rata share of all overhead costs attributable to the manufacture of the property.
- (4) Reasonable profit from the manufacturing operations which, in the absence of evidence to the contrary, shall be deemed to be 5 percent of the sum of the factors listed in subsections (1) to (3), inclusive.

~~(f) OPERATIVE DATE.~~ All provisions of this regulation cease to be operative as of January 1, 2004, as provided by Revenue and Taxation Code section 6377(g). Retailers and qualified persons may not accept or claim any Section 6377 Manufacturer’s Exemption Certificates for a sale or use made after December 31, 2003.

Tuesday, April 22, 2014

AT&T Mobility, LLC, (2606)

2010 to 2013, \$572,462.00 Unitary Value

Action: Upon motion of Mr. Runner, seconded by Ms. Yee and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee and Mr. Runner voting yes, Ms. Mandel not participating in accordance with Government Code section 7.9, the Board adopted the unitary land escaped assessment as recommended by staff.

Board Roll Changes

2010, 2011, 2012 and 2013 State-Assessed Property Rolls

Action: Upon motion of Mr. Runner, seconded by Ms. Yee and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee and Mr. Runner voting yes, Ms. Mandel not participating in accordance with Government Code section 7.9, the Board approved corrections to the 2010, 2011, 2012 and 2013 Board Rolls of State-Assessed Property as recommended by staff (Exhibit 4.9).

CHIEF COUNSEL MATTERS**RULEMAKING****Section 100 Changes*****Sales and Use Tax Regulations 1525.2, Manufacturing Equipment; and, 1525.3, Manufacturing Equipment – Leases of Tangible Personal Property***

Bradley Heller, Tax Counsel, Tax and Fee Programs Division, Legal Department, made introductory remarks regarding the staff request for authorization to complete Rule 100 changes to repeal Regulations 1525.2 and 1525.3 based on the repeal of Revenue and Taxation Code section 6377 by its own terms effective January 1, 2004 (Exhibit 4.10).

Action: Upon motion of Mr. Runner, seconded by Ms. Yee and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee, Mr. Runner and Ms. Mandel voting yes, the Board approved authorization to make Rule 100 changes to Regulations 1525.2 and 1525.3 as recommended by staff.

ADMINISTRATIVE SESSION**ADMINISTRATIVE MATTERS, CONSENT**

With respect to the Administrative Matters, Consent Agenda, upon a single motion of Ms. Steel, seconded by Ms. Yee and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee, Mr. Runner and Ms. Mandel voting yes, the Board made the following orders:

BEFORE THE CALIFORNIA STATE BOARD OF EQUALIZATION

450 N STREET
SACRAMENTO, CALIFORNIA

REPORTER'S TRANSCRIPT

APRIL 22, 2014

CHIEF COUNSEL MATTERS

J RULEMAKING

J1 SALES AND USE TAX REGULATIONS

1525.2 MANUFACTURING EQUIPMENT

1525.3 MANUFACTURING EQUIPMENT

LEASES OF TANGIBLE PERSONAL PROPERTY

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Reported by: Juli Price Jackson

No. CSR 5214

P R E S E N T

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For the Board
of Equalization:

Jerome E. Horton
Chairman

Michelle Steel
Vice-Chairwoman

Betty T. Yee
Member

George Runner
Member

Marcy Jo Mandel
Appearing for
John Chiang,
State Controller
(per Government
Code Section 7.9)

Joann Richmond
Chief, Board
Proceedings
Division

For Staff:

Bradley Heller
Tax Counsel IV
Legal Department

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1 450 N STREET
2 SACRAMENTO, CALIFORNIA
3 APRIL 22, 2014

4 ---oOo---

5 MS. RICHMOND: Our next item is Chief
6 Counsel Matters, J, Rulemaking, Section 100 change,
7 J1, Sales and Use Tax Regulations 1525.2,
8 manufacturing equipment and 1525.3, manufacturing
9 equipment, leases of tangible personal property.

10 MR. HORTON: Thank you.

11 Mr. Heller, would you please introduce the
12 issues in this case?

13 MR. HELLER: Good evening, Chairman
14 Horton --

15 MR. HORTON: Good evening.

16 MR. HELLER: -- Members of the Board, I'm
17 Bradley Heller from the Board's Legal Department.

18 I am here to request that the Board vote to
19 authorize Rule 100 changes to repeal Sales and Use
20 Tax Regulations 1525.2, manufacturing equipment, and
21 1525.3, manufacturing equipment, leases of tangible
22 personal property.

23 MR. HORTON: Discussion?

24 MR. RUNNER: Adopt.

25 MR. HORTON: Discussion, Members.
26 Member Runner.

27 MR. RUNNER: Move to adopt.

28 MR. HORTON: Member Runner moves to adopt

1 staff recommendation to authorize staff to complete
2 Rule 100 changes to repeal.

3 Second by Member Steel -- Yee.

4 Without objection, Members, such will be
5 the order.

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REPORTER'S CERTIFICATE.

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State of California)
) ss
County of Sacramento)

I, JULI PRICE JACKSON, Hearing Reporter for
the California State Board of Equalization certify
that on APRIL 22, 2014 I recorded verbatim, in
shorthand, to the best of my ability, the
proceedings in the above-entitled hearing; that I
transcribed the shorthand writing into typewriting;
and that the preceding pages 1 through 4 constitute
a complete and accurate transcription of the
shorthand writing.

Dated: MAY 1, 2014



JULI PRICE JACKSON
Hearing Reporter

