

Rulemaking File Index
Title 18. Public Revenue
Sales and Use Tax
Regulation 1618 *United States Government Supply Contracts*

OAL Approval

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**State of California
Office of Administrative Law**

In re:
Board of Equalization

**NOTICE OF APPROVAL OF REGULATORY
ACTION**

Regulatory Action:

Government Code Section 11349.3

Title 18, California Code of Regulations

OAL File No. 2012-0713-02 S

Adopt sections:
Amend sections: 1618
Repeal sections:

The State Board of Equalization proposed to amend section 1618 of title 18 of the California Code of Regulations to provide that effective June 14, 2007, the word "tools" as used in the definition of "Direct consumable supplies" shall include "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17 and to make other clarifying changes. The change described above is being made to conform to changes made to the Code of Federal Regulations in 2007 repealing FAR 52.245-17.

OAL approves this regulatory action pursuant to section 11349.3 of the Government Code. This regulatory action becomes effective on 9/6/2012.

RAIG TARPENNING

Date: 8/7/2012

Craig S. Tarpenning
Senior Staff Counsel

For: DEBRA M. CORNEZ
Director

Original: Kristine Cazadd
Copy: Richard Bennion

RECEIVED

AUG - 8 2012

**State of California
Office of Administrative Law**

by EXECUTIVE DIRECTOR'S OFFICE
STATE BOARD OF EQUALIZATION

In re:
Board of Equalization

**NOTICE OF APPROVAL OF REGULATORY
ACTION**

Regulatory Action:

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Title 18, California Code of Regulations

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Craig S. Tarpinning
Senior Staff Counsel

For: DEBRA M. CORNEZ
Director

Original: Kristine Cazadd
Copy: Richard Bennion

OFFICE OF ADMINISTRATIVE LAW

300 Capitol Mall, Suite 1250
Sacramento, CA 95814
(916) 323-6225 FAX (916) 323-6826



DEBRA M. CORNEZ
Director

MEMORANDUM

TO: Richard Bennion
FROM: OAL Front Desk 
DATE: 8/9/2012
RE: Return of Approved Rulemaking Materials
OAL File No. 2012-0713-02S

OAL hereby returns this file your agency submitted for our review (OAL File No. 2012-0713-02S regarding United States Government Supply Contracts).

If this is an approved file, it contains a copy of the regulation(s) stamped "ENDORSED APPROVED" by the Office of Administrative Law and "ENDORSED FILED" by the Secretary of State. The effective date of an approved file is specified on the Form 400 (see item B.5). (Please Note: The 30th Day after filing with the Secretary of State is calculated from the date the Form 400 was stamped "ENDORSED FILED" by the Secretary of State.)

DO NOT DISCARD OR DESTROY THIS FILE

Due to its legal significance, you are required by law to preserve this rulemaking record. Government Code section 11347.3(d) requires that this record be available to the public and to the courts for possible later review. Government Code section 11347.3(e) further provides that "...no item contained in the file shall be removed, altered, or destroyed or otherwise disposed of." See also the Records Management Act (Government Code section 14740 et seq.) and the State Administrative Manual (SAM) section 1600 et seq.) regarding retention of your records.

If you decide not to keep the rulemaking records at your agency/office or at the State Records Center, you may transmit it to the State Archives with instructions that the Secretary of State shall not remove, alter, or destroy or otherwise dispose of any item contained in the file. See Government Code section 11347.3(f).

Enclosures

STD. 400 (REV. 01-09)

OAL FILE NUMBERS	NOTICE FILE NUMBER Z-2012-0406-01	REGULATORY ACTION NUMBER 2012-0713-02 S	EMERGENCY NUMBER
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For use by Office of Administrative Law (OAL) only

ENDORSED FILED
OFFICE OF
2012 AUG -7 PM 4:28
[Signature]
SECRETARY OF STATE

<p>2012 JUL 13 A 10:53</p> <p>OFFICE OF ADMINISTRATIVE LAW</p>	<p>NOTICE</p>
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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 2012, 16-2	PUBLICATION DATE 7/20/2012

B. SUBMISSION OF REGULATIONS (Complete when submitting regulations)

1a. SUBJECT OF REGULATION(S) United States Government Supply Contracts	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 1618
	REPEAL
TITLE(S) 18	

3. TYPE OF FILING

<input checked="" 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 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 checked="" type="checkbox"/> Effective 30th day after filing with Secretary of State	<input type="checkbox"/> Effective on filing with Secretary of State	<input 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
---	------------------------------------	---	--

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 July 11, 2012
TYPED NAME AND TITLE OF SIGNATORY Joann Richmond, Chief, Board Proceedings Division	

For use by Office of Administrative Law (OAL) only

ENDORSED APPROVED

AUG 27 2012

(Initials and Date)

**Final Text of Proposed Amendments to
California Code of Regulations, Title 18, Section 1618**

Section 1618. United States Government Supply Contracts.

(a) Definitions.

(1) "United States Government supply contract" means a contract with the United States to furnish, or to fabricate and furnish, tangible personal property including ships, aircraft, ordnance, or equipment, whereby title to tangible personal property purchased for use in fulfilling the contract passes to the United States pursuant to the title provisions contained in the contract before the contractor uses the property to perform the function or act for which the property was designed or manufactured. The term "U.S. Government supply contract" does not include contracts to construct improvements on or to real property or to the purchase of tangible personal property for use in fulfilling such contracts.

(2) "Direct consumable supplies" means supplies, tools, or equipment consumed in the performance of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~"Tools" as used in this definition does not include "special tooling" subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17. Effective June 14, 2007, "Tools" as used in this definition includes "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.~~

(3) "Overhead materials" means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

(2) Whether title to direct consumable supplies ~~and/or indirect consumable supplies (i.e., overhead materials)~~ passes to the United States under a United States government supply contract and the time at which title passes will be determined in

accordance with the title provisions contained in the contract, if any. ~~In a case where the cost of~~

(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

(B) For indirect consumable supplies (i.e., overhead materials), which are charged to an expense account which is then allocated to various locations, cost centers or contracts, ~~some of which are engaged in other than United States government cost reimbursement contracts and/or fixed price contracts with a progress payments clause,~~ it will be considered that title ~~did not pass~~ to the United States government prior to use of the property, and tax will not apply with respect to the purchase or use of the property charged to the expense account, unless the item is specifically accounted for as being charged allocated to a specific United States government supply contract, pursuant to the terms of which title passes to the United States prior to the use of the item. Property will be considered charged allocated to a specific United States government supply contract when it is allocated pursuant to:

~~(1) a1.~~ Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,

~~(2) g2.~~ Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in ~~this~~ the manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

(3) Special Tooling. Effective December 29, 1989 through June 13, 2007, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17. Title to such special tooling will pass prior to use by the contractor only if the agreement between the contractor and the United States government contains a custom clause providing for title passage prior to use by the contractor. Therefore, sales of special tooling will generally be subject to tax.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6007 and 6381, Revenue and Taxation Code; and Aerospace Corp. v. St. Bd. of Equalization (1990) 218 Cal.App.3d 1300.

LEV III program in 2018; establishing more stringent particulate matter standards for light- and medium-duty vehicles; establishing zero fuel evaporative emission standards for passenger cars and light-duty trucks, and more stringent evaporative standards for medium-duty vehicles; establishing more stringent supplemental federal test procedure (SFTP) standards for passenger cars and light-duty trucks; and, for the first time, requiring medium-duty vehicles to meet SFTP standards.

Other minor amendments (e.g., in-use verification testing requirements, reporting requirements, etc.) are proposed to align existing related procedures with the principal amendments. These amendments also establish more stringent greenhouse gas regulations that are comprised of three emission standards; use a footprint-based approach to reduce emissions from new light-duty vehicles and medium-duty passenger vehicles; provide credits for improvements to the vehicle air conditioning system (either from the use of a refrigerant with a low Global Warming Potential or by incorporating improvements to the efficiency of the system); provide credits for technologies that reduce CO₂ emissions but are not measured on the applicable test cycles; and provide credits for technology innovations on the largest of pickup trucks.

Title 13
California Code of Regulations
ADOPT: 1961.2, 1961.3 AMEND: 1900, 1956.8,
1960.1, 1961, 1961.1, 1965, 1968.2, 1968.5, 1976,
1978, 2037, 2038, 2062, 2112, 2139, 2140, 2145,
2147, 2235, 2317
Filed 08/07/2012
Effective 08/07/2012
Agency Contact: Trini Balcazar (916) 445-9564

File# 2012-0625-04
AIR RESOURCES BOARD
Zero Emission Vehicles 2012 Amendments

This regulatory action amends regulations that require automobile manufacturers to develop and commercialize zero emission vehicle (ZEV) technologies. These include: increases ZEV percentage requirements for model years 2018 through 2025; increases flexibility for manufacturers to comply with ZEV requirements; simplifies the credit system for ZEVs and plug-in hybrid electric vehicles (PHEVs); and creates an optional compliance path for manufacturers in Section 177 states.

Title 13
California Code of Regulations
ADOPT: 1962.2 AMEND: 1962.1, 1962.2 (renu-
mered to 1962.3)
Filed 08/07/2012
Effective 08/07/2012
Agency Contact: Amy Whiting (916) 322-6533

File# 2012-0713-02
BOARD OF EQUALIZATION
United States Government Supply Contracts

The State Board of Equalization amended section 1618 of title 18 of the California Code of Regulations to provide that effective June 14, 2007, the word "tools" as used in the definition of "Direct consumable supplies" shall include "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17 and to make other clarifying changes. The change described above is being made to conform to changes made to the Code of Federal Regulations in 2007 repealing FAR 52.245-17.

Title 18
California Code of Regulations
AMEND: 1618
Filed 08/07/2012
Effective 09/06/2012
Agency Contact:
Richard E. Bennion (916) 445-2130

File# 2012-0726-02
**CALIFORNIA DEBT LIMIT ALLOCATION
COMMITTEE**
Administration of California's Limited Tax-Exempt
Debt Authority

The California Debt Limit Allocation Committee (CDLAC) readopted an emergency regulation that amended section 5052 of title 4 of the California Code of Regulations to allow the full refund of the performance deposit if 80% or more of the Allocation is used to issue bonds or issue at least one (1) Mortgage Credit Certificate prior to the expiration date.

Title 4
California Code of Regulations
AMEND: 5000, 5052
Filed 08/01/2012
Effective 08/01/2012
Agency Contact: Annie Ong (916) 653-8018

Rulemaking File Index
Title 18. Public Revenue
Sales and Use Tax
Regulation 1618 *United States Government Supply Contracts*

1. [Final Statement of Reasons](#)
2. [Updated Informative Digest](#)
3. [Business Tax Committee Minutes, March 20, 2012](#)
 - Minutes and Proposed Text
 - BTC Agenda
 - Formal Issue Paper 12-001
 - Exhibit 1 Revenue Estimate
 - Exhibit 2 Text Regulation 1618
4. [Reporter's Transcript Business Taxes Committee, March 20, 2012](#)
5. [Estimate of Cost or Savings, April 6, 2012](#)
6. [Economic and Fiscal Impact Statements, April 5, 2012](#)
7. [Notice of Publications](#)
 - Form 400 and Notice, Publication Date April 20, 2012
 - Proposed Text of Regulation 1618
 - Email sent to Interested Parties, April 20, 2012
 - CA Regulatory Notice Register 2012, Volume No. 16-Z
8. [Notice to Interested Parties, April 20, 2012](#)

The following items are exhibited:

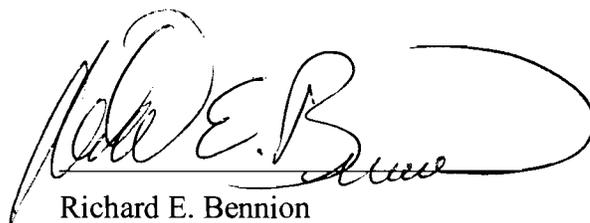
 - Notice of Hearing
 - Initial Statement of Reasons
 - Proposed Text of Regulation 1618
 - Regulation History
9. [Statement of Compliance](#)
10. [Reporter's Transcript, Item F3, June 26, 2012](#)
11. [Draft Minutes, June 26, 2012, and Exhibits](#)
 - Notice of Proposed Regulatory Action
 - Initial Statement of Reasons
 - Proposed Text of Regulation 1618
 - Regulation History

VERIFICATION

I, Richard E. Bennion, Regulations Coordinator of the State Board of Equalization, state that the rulemaking file of which the contents as listed in the index is complete, and that the record was closed on July 11, 2012 and that the attached copy is complete.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

July 11, 2012

A handwritten signature in black ink, appearing to read "Richard E. Bennion", with a large, sweeping flourish extending to the right.

Richard E. Bennion
Regulations Coordinator
State Board of Equalization

**Final Statement of Reasons for
Adoption of Proposed Amendments to California Code of Regulations,
Title 18, Section 1618, *United States Government Supply Contracts***

Update of Information in the Initial Statement of Reasons

The factual basis, specific purpose, and necessity for, and the anticipated benefits from, the proposed amendments to California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*, are the same as provided in the initial statement of reasons.

The adoption of the proposed amendments to Regulation 1618 was not mandated by federal law or regulations and there is no federal regulation that is identical to Regulation 1618, although changes to federal regulations are one of the reasons why the proposed amendments are necessary.

The State Board of Equalization (Board) did not rely on any data or any technical, theoretical, or empirical study, report, or similar document in proposing or adopting the amendments to Regulation 1618 that was not identified in the initial statement of reasons, or which was otherwise not identified or made available for public review prior to the close of the public comment period.

In addition, the factual basis has not changed for the Board's initial determination that the proposed regulatory action will not have a significant adverse economic impact on business and the Board's economic impact analysis, which determined that the Board's proposed regulatory action:

- Will neither create nor eliminate jobs in the State of California;
- Nor result in the elimination of existing businesses;
- Nor create or expand business in the State of California; and
- Will not affect the health and welfare of California residents, worker safety, or the state's environment.

The proposed amendments may affect small business.

No Mandate on Local Agencies or School Districts

The Board has determined that the adoption of the proposed amendments to Regulation 1618 does not impose a mandate on local agencies or school districts.

Public Comments

The Board did not receive any written comments regarding the proposed amendments to Regulation 1618 and no interested parties asked to speak at the public hearing on June 26, 2012.

Determinations Regarding Alternatives

By its motion, the Board determined that no alternative to the proposed amendments to Regulation 1618 would be more effective in carrying out the purposes for which the regulation is proposed, would be as effective and less burdensome to affected private persons than the adopted regulation, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provisions of law.

Further, the Board did not reject any reasonable alternatives to the proposed amendments to Regulation 1618 that would lessen any adverse impact the proposed amendments may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed amendments. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

Furthermore, the Aerospace Industries Association (AIA) participated in the development of and agreed with the proposed amendments to Regulation 1618, as set forth in Formal Issue Paper 12-001. And, the Board's proposed amendments are anticipated to provide the following benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to chapter 1 of title 48 of the Code of Federal Regulations, the Federal Acquisition Regulation (FAR), effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

Updated Informative Digest for
Adoption of Proposed Amendments to California Code of Regulations,
Title 18, Section 1618, *United States Government Supply Contracts*

On June 26, 2012, the State Board of Equalization (Board) held a public hearing on and unanimously voted to adopt the original text of the proposed amendments to California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*, described in the notice of proposed regulatory action. There have not been any changes to the applicable laws or the effect of the adoption of the proposed amendments to Regulation 1618 described in the informative digest included in the notice of proposed regulatory action. The Board did not receive any written comments regarding the proposed amendments to Regulation 1618 and no interested parties appeared at the public hearing on June 26, 2012.

The informative digest included in the notice of proposed regulatory action provides:

“Current Regulation 1618

“Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, RTC section 6007 provides that the term ‘retail sale’ means ‘a sale for any purpose other than resale in the regular course of business’ and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

“Regulation 1618 currently prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor’s business (hereafter, ‘sales for resale to the United States’). The regulation generally provides that:

- A retailer’s sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer’s sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

“Regulation 1618 also currently provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in the FAR, and Regulation 1618 provides specific guidance as to when title to ‘special tooling’ passes to the United States under the FAR.

“2007 Amendments to FAR

“Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal’s decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to ‘special tooling’ passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for ‘special tooling,’ and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007.

“Effect, Objectives, and Benefits of the Proposed Amendments to Regulation 1618

“The Board directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts. At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR, and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term ‘tools,’ as used in the definition of direct consumable supplies, does not include ‘special tooling’;
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term ‘tools,’ as used in the definition of direct consumable supplies, includes ‘special tooling’ that ‘was previously covered by FAR part 52.245-17’; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR’s title passage clauses for special tooling applied until Jun 13, 2007, but were no longer effective after that date.

“In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for ‘overhead materials’ must be allocated to United States Government supply contracts ‘consistent with government cost accounting standards.’ It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to ‘direct consumable supplies’ and ‘overhead materials’ by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of ‘indirect consumable supplies,’ and providing distinct guidance regarding the passage of title to direct consumable

supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

“The Aerospace Industries Association (AIA) participated in Board staff’s meetings with the interested parties and AIA agreed with staff’s recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

“During its March 20, 2012, Business Taxes Committee meeting, the Board determined that staff’s recommended amendments are reasonably necessary to accomplish the objectives of making Regulation 1618 consistent with the 2007 amendments to the FAR and clarifying Regulation 1618’s guidance regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials. The proposed amendments are anticipated to provide the following specific benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

“The Board has performed an evaluation of whether the proposed amendments to Regulation 1618 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1618 is the only state regulation prescribing the requirements for making sales for resale to the United States. In addition, there is no federal sales tax and there are no comparable federal regulations or statutes to Regulation 1618.”



**BOARD OF EQUALIZATION
BUSINESS TAXES COMMITTEE MEETING MINUTES**

HONORABLE BETTY T. YEE, COMMITTEE CHAIR

450 N STREET, SACRAMENTO

MEETING DATE: MARCH 20, 2012, TIME: 10:00 A.M.

ACTION ITEMS & STATUS REPORT ITEMS

Agenda Item No: 1

Title: Proposed amendments to Regulation 1618, *United States Government Supply Contracts*

Issue/Topic:

Request approval and authorization to publish proposed amendments to conform the regulation to changes in the Federal Acquisition Regulation (FAR).

Committee Discussion:

There was no discussion of this item.

Committee Action:

Upon motion by Mr. Horton, seconded by Ms. Mandel, without objection, the Committee approved and authorized for publication the proposed amendments to Regulation 1618.

The proposed amendments will not have an operative date. Implementation will take place 30 days after approval by the Office of Administrative Law. A copy of the proposed amendments is attached.

Agenda Item No: 2

Title: Proposed revisions to sections 901.000 through 906.000 of Compliance Policy and Procedures Manual Chapter 9, *Miscellaneous*

Issue/Topic:

Request approval of proposed procedure manual revisions regarding local and district tax reallocations.

Committee Discussion:

Action 1, Consent

There was no discussion of this item.

Committee Action:Action 1, Consent

Upon motion by Mr. Horton, seconded by Ms. Steel, the Committee unanimously approved the consent item.

Committee Discussion:Action 2, Requirement that designated person provides a copy of its contract with the jurisdiction (901.020, 901.030, 901.040, and 905.010)

Staff's recommendation provided that a copy of the contract between the jurisdiction and the representative must be provided before the representative is given access to BOE records. MuniServices, LLC's (MuniServices) recommendation did not include this requirement.

Interested parties explained that they have no objection to providing BOE with a copy of their contract, but they disagree that Revenue and Taxation Code section 7056 requires the contract be provided. Staff explained that while the statute does not specifically state the contract be provided, staff cannot ensure that the requirements of the statute have been met without reviewing the contract.

Committee Action:Action 2, Requirement that designated person provides a copy of its contract with the jurisdiction (901.020, 901.030, 901.040, and 905.010)

Upon motion by Ms. Mandel, seconded by Mr. Horton, the Committee unanimously approved staff's recommendation that a copy of the contract between the jurisdiction and the representative be provided before the representative is given access to BOE records.

Committee Discussion:Action 3, Threshold for processing fund transfers (905.020)

Staff proposed that the minimum threshold for processing fund transfers be raised from \$50 per quarter to \$250 per quarter. The HdL Companies (HdL) proposed that the threshold be set at \$100 per quarter, and MuniServices proposed that the threshold be set at \$50 per quarter or \$250 for the entire period in dispute, whichever is less.

Interested parties explained the staff proposal is an excessive increase over the current threshold and would be detrimental to jurisdictions, particularly small cities. They further explained that jurisdictions are BOE's customers and it is unfair to deny them local tax dollars because of staff's workload concerns. Staff explained that small reallocation adjustments require significant staff resources and that those resources would be better spent investigating petitions involving larger dollar amounts. Staff further explained that the staff proposal is consistent with other sales and use tax audit processing thresholds. Board Members discussed BOE's responsibility to ensure that jurisdictions receive funds they are entitled to, and that small errors should be corrected because they could increase to significant tax amounts over time. Board Members also expressed interest in learning staff workload impacts at the different thresholds and how staff believes local jurisdictions would benefit from the staff proposal.

Committee Action:Action 3, Threshold for processing fund transfers (905.020)

Upon motion by Mr. Runner, seconded by Ms. Mandel, the Committee unanimously approved the motion to move this action item over for further review and discussion.

Committee Discussion:Action 4, Timeframes to acknowledge submissions (905.030)

Staff proposed that the Allocation Group acknowledge submissions intended as petitions within 30 calendar days of receipt. MuniServices proposed the submissions be acknowledged within seven calendar days of receipt.

There was no discussion of this item.

Committee Action:Action 4, Timeframes to acknowledge submissions (905.030)

Upon motion by Mr. Runner, seconded by Mr. Horton, the Committee unanimously approved staff's recommendation to allow 30 calendar days for Allocation Group staff to acknowledge submissions intended as petitions.

Committee Discussion:Action 5, Documenting a Date of Knowledge (905.040)

Staff's recommendation explained when a Date of Knowledge is operationally documented by BOE staff. MuniServices' proposed language provided that staff must include the information required under Regulation 1807 that supports the probability of a misallocation and staff should contact the taxpayer to establish that there is a basis for questioning the reported allocation, unless circumstances do not warrant that contact.

Staff and interested parties agree that staff should meet the same standards when staff operationally documents a date of knowledge as jurisdictions must meet when they file a petition. MuniServices explained that they believe it is important the CPPM section reference the requirements of Regulation 1807, but agreed to drop their suggested language about staff contacting the taxpayer before operationally documenting a date of knowledge.

Committee Action:Action 5, Documenting a Date of Knowledge (905.040)

Upon motion by Mr. Runner, seconded by Mr. Horton, the Committee unanimously approved the motion to modify staff's proposed language to provide that to operationally document a date of knowledge, staff must provide sufficient factual data consistent with the definition of a petition in Regulation 1807.

Committee Discussion:Action 6, Allocation Group supervisor follow-up timeframes (905.050)

Staff proposed that the Allocation Group lead follow up on assignments aged 180-270 days and the Allocation Group supervisor follow up on assignments aged greater than 270 days. MuniServices proposed that the Allocation Group lead follow up at 90-180 days and the Allocation Group supervisor follow up after 180 days.

Interested parties explained they suggested their timeframes because they thought it would be better for the Allocation Group lead and supervisor to review a case prior to the first trigger provision in Regulation 1807 which allows a jurisdiction to request the Allocation Group issue their decision within 90 days. Staff explained that the staff suggested timeframes are intended to be outside time limits.

Committee Action:Action 6, Allocation Group supervisor follow-up timeframes (905.050)

Upon motion by Mr. Horton, seconded by Mr. Runner, the Committee unanimously approved staff's recommendation that the Allocation Group lead follow up on assignments aged 180-270 days and the Allocation Group supervisor follow up on assignments aged greater than 270 days.

Committee Discussion:Action 7, Informing jurisdictions prior to processing a large deallocation of local tax resulting from a refund or credit in an audit (907.000)

Staff proposed that staff inform jurisdictions when a pending refund or credit in an audit results in a deallocation of \$100,000 or more in local tax to a jurisdiction. MuniServices and HdL proposed that a jurisdiction be informed when a pending refund or credit in an audit results in a deallocation of \$50,000 or more in local tax to a jurisdiction.

Interested parties explained that the lower threshold would help small cities plan better, because \$50,000 in local tax is significant to a small city. Mr. Runner stated that information provided to his office indicated that, using the refund cases brought before the Board in the last year, the \$50,000 threshold resulted in only 12 additional notifications than the \$100,000 threshold. Staff explained the work that needs to be done to determine if notification is necessary is a manual process and could be time intensive depending on the complexity of the transactions in the audit or claim for refund.

Committee Action:Action 7, Informing jurisdictions prior to processing a large deallocation of local tax resulting from a refund or credit in an audit (907.000)

Upon motion by Mr. Runner, seconded by Mr. Horton, the Committee unanimously approved HdL's and MuniServices recommendation to inform jurisdictions when a pending refund or credit in an audit results in a deallocation of \$50,000 or more in local tax to a jurisdiction.

Agenda Item No: 3**Title: Technology Transfer Agreements****Issue/Topic:**

Study update and request for an interested parties process.

Committee Discussion:

Staff provided an update on actions taken by staff and the results of contact letters sent to prospective study participants.

Staff also requested approval for an interested parties process to determine whether Regulation 1507, *Technology Transfer Agreements*, should be amended to clarify when sales or purchases of software qualify as technology transfer agreements and how tax applies to sales of qualifying software media.

Interested parties indicated support for moving forward with the interested parties process.

Committee Action:

Upon motion by Mr. Runner, seconded by Mr. Horton, the Committee unanimously approved staff to begin the interested parties process to discuss Regulation 1507. Due to the sensitivity of the issue, Ms. Yee requested an update be provided to the Board after the first interested parties meeting.

/s/ Betty T. Yee

Honorable Betty T. Yee, Committee Chair

/s/ Kristine Cazadd

Kristine Cazadd, Executive Director

BOARD APPROVED

at the March 21, 2012 Board Meeting

/s/ Diane Olson

Diane Olson, Chief
Board Proceedings Division

Regulation 1618. United States Government Supply Contracts.

(a) Definitions.

(1) "United States Government supply contract" means a contract with the United States to furnish, or to fabricate and furnish, tangible personal property including ships, aircraft, ordnance, or equipment, whereby title to tangible personal property purchased for use in fulfilling the contract passes to the United States pursuant to the title provisions contained in the contract before the contractor uses the property to perform the function or act for which the property was designed or manufactured. The term "U.S. Government supply contract" does not include contracts to construct improvements on or to real property or to the purchase of tangible personal property for use in fulfilling such contracts.

(2) "Direct consumable supplies" means supplies, tools, or equipment consumed in the performance of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~"Tools" as used in this definition does not include "special tooling" subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17. Effective June 14, 2007. "Tools" as used in this definition includes "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.~~

(3) "Overhead materials" means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

(2) Whether title to direct consumable supplies and/or indirect consumable supplies (i.e., overhead materials) passes to the United States under a United States government supply contract and the time at which title passes will be determined in accordance with the title provisions contained in the contract, if any. ~~In a case where the cost of~~

(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

~~(A)(B)~~ F—or indirect consumable supplies (i.e., overhead materials) which are charged to an expense account which is then allocated to various locations, cost centers or contracts, some of which are engaged in other than United States government cost reimbursement contracts and/or fixed price contracts with a progress payments clause. it will be considered that title ~~did not pass~~ passed to the United States government prior to use of the property, and tax will not apply with respect to the purchase or use of the property charged to the expense account, unless if the item is specifically accounted for as being charged allocated to a specific United States government supply contract, pursuant to the terms of which title passes to the United States prior to the use of the item. Property will be considered ~~charged~~ allocated to a specific United States government supply contract when it is allocated pursuant to:

~~(1)~~ 1. Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,

~~(2)~~ 2. Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in this the manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

~~(2)(3)~~ Special Tooling. Effective December 29, 1989 through June 13, 2007, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17. Title to such special tooling will pass prior to use by the contractor only if the agreement between the contractor and the United States government contains a custom clause providing for title passage prior to use by the contractor. Therefore, sales of special tooling will generally be subject to tax.

Reference: Sections 6007 and 6381, Revenue and Taxation Code.

Aerospace Corp. v. St. Bd. of Equalization (1990) 218 Cal.App.3d 1300.



BOARD OF EQUALIZATION

BUSINESS TAXES COMMITTEE MEETING AGENDA

HONORABLE BETTY YEE, COMMITTEE CHAIRWOMAN

450 N STREET, SACRAMENTO - ROOM 121

MARCH 20, 2012 – 10:00 A.M.

1. Proposed amendments to Regulation 1618, *United States Government Supply Contracts*

Request authorization to publish proposed amendments to conform the regulation to changes in the Federal Acquisition Regulation (FAR)

2. Proposed revisions to sections 901.000 through 906.000 of Compliance Policy and Procedures Manual Chapter 9, *Miscellaneous*

Request approval of proposed procedure manual revisions regarding local and district tax reallocations

3. Technology Transfer Agreements

Project update and request to initiate an interested parties process

AGENDA — March 20, 2012 Business Taxes Committee Meeting
Proposed Amendments to Regulation 1618, *United States Government Supply Contracts*

of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~“Tools” as used in this definition does not include “special tooling” subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17. Effective June 14, 2007, “Tools” as used in this definition includes “special tooling” that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.~~

(3) “Overhead materials” means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

(2) Whether title to direct consumable supplies and/or indirect consumable supplies (i.e., overhead materials) passes to the United States under a United States government supply contract and the time at which title passes will be determined in accordance with the title provisions contained in the contract, if any. In a case where the cost of

(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

~~(A)~~ (B) For indirect consumable supplies (i.e., overhead materials) which are charged to an expense account which is then allocated to various locations, cost centers or contracts,

AGENDA — March 20, 2012 Business Taxes Committee Meeting
Proposed Amendments to Regulation 1618, *United States Government Supply Contracts*

~~some of which are engaged in other than United States government cost reimbursement contracts and/or fixed price contracts with a progress payments clause. it will be considered that title did not pass to the United States government prior to use of the property, and tax will not apply with respect to the purchase or use of the property charged to the expense account, unless if the item is specifically accounted for as being charged~~ allocated to a specific United States government supply contract, pursuant to the terms of which title passes to the United States prior to the use of the item. Property will be considered ~~charged~~ allocated to a specific United States government supply contract when it is allocated pursuant to:

- ~~(1)~~ 1. Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,
- ~~(2)~~ 2. Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in ~~this the~~ manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

Special Tooling. Effective December 29, 1989 through June 13, 2007, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17. Title to such special tooling will pass prior to use by the contractor only if the agreement between the contractor and the United States government contains a custom clause providing for title passage prior to use by the contractor. Therefore, sales of special tooling will generally be subject to tax.

Issue Paper Number **12-001**



BOARD OF EQUALIZATION
KEY AGENCY ISSUE

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

Proposed Amendments to Regulation 1618, *United States Government Supply Contracts*

I. Issue

Should Regulation 1618, *United States Government Supply Contracts*, be amended to conform the regulation to changes in the Federal Acquisition Regulation (FAR)?

II. Alternative 1 - Staff Recommendation

Staff recommends the Board approve and authorize publication of proposed amendments to Regulation 1618 to:

- Address the deletion of FAR 52.245-17, *Special Tooling*,
- Separate for clarity the discussion of the application of tax on purchases of direct consumable supplies and indirect consumable supplies, and
- Update the wording throughout the regulation for clarity.

Mr. Joe Vinatieri and the Aerospace Industries Association (AIA) agree on the proposed amendments. The proposed amendments are attached as Exhibit 2.

III. Other Alternative Considered

Do not amend Regulation 1618.

Issue Paper Number 12-001

IV. Background

FAR is the United States Government regulation governing the “acquisition process,” which is the process through which the government purchases goods and services, including the passage of title to the United States Government when purchasing goods from government supply contractors. FAR Parts 1 through 51 discuss policies and procedures and Part 52 provides the clauses that are inserted into contracts. FAR is updated regularly but in 2007 there was a major rewrite of Part 45, *Government Property*, and the related clauses in Part 52.2, *Text of Provisions and Clauses*. Several government property clauses were combined into one clause. Regulation 1618 provides guidelines for the application of tax to purchases and sales made by United States Government supply contractors and references FAR. The regulation was last amended in 1995 to incorporate the decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, which provided that title to overhead materials passes to the government prior to use when the appropriate title clauses are in the contract. Procedures for auditing government supply contractors are included in Audit Manual sections 0411.00 through 0411.25 and Exhibits 10A through 10F. The audit manual sections discuss the application of tax to direct and indirect consumable supplies based on the type of contract (fixed price or cost-type) and the specific title clauses included in the contract.

Staff recommends Regulation 1618 be updated to reflect the new consolidated clause under FAR 52.245-1 and the deletion of the separate clauses for “special tooling” and “special test equipment.”

Staff met with interested parties on August 18, 2011, November 29, 2011, and January 17, 2012, to discuss and refine the proposed changes to the regulation. At these meetings, staff and interested parties also discussed revisions to Audit Manual Chapter 4, sections 0411.00 through 0411.25 and Exhibits 10A through 10F, to reflect the changes to FAR. The proposed revisions to the audit manual have been postponed until the May 2012 Business Taxes Committee meeting to allow staff and interested parties to further discuss and possibly resolve some of the outstanding audit procedure issues.

The proposed amendments to Regulation 1618 are scheduled for discussion at the March 20, 2012 meeting of the Business Taxes Committee.

V. Discussion

Regulation 1618 – Exhibit 2

Revisions Based on Changes to FAR

In the 2007 FAR rewrite, FAR 52.245-17, *Special Tooling*, was deleted. However, subdivision (a)(2) of Regulation 1618 currently provides in part:

“Tools” as used in this definition does not include “special tooling” subject to the provisions of Federal Acquisition Regulation (FAR) 52-245-17 or any regulation(s) which succeeds FAR 52.245-17.

In addition, subdivision (b)(2) of the regulation currently provides, in part:

Special Tooling. Effective December 29, 1989, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17.

Issue Paper Number 12-001

Staff and AIA propose to amend the regulation to reflect the deletion of FAR 52.245-17. Following the deletion of FAR 52.245-17, special tooling is included in “direct consumable supplies” as defined by the regulation.

Revisions Recommended for Clarity

Before the *Aerospace* decision, the regulation separately discussed the application of tax to sales of direct consumable supplies and indirect consumable supplies. When the regulation was amended after the decision, the discussion of the application of tax to direct consumable supplies was combined with the discussion of the application of tax to indirect consumable supplies. Staff and AIA agree that clarification is needed in this area and propose reorganizing subdivision (b) and rewording the discussion of indirect consumable supplies (overhead materials) to provide clarification of whether title passes to the United States Government prior to use.

Non-substantive Changes to the Regulation

In addition, staff and AIA propose various non-substantive grammatical changes and corrections throughout the regulation.

VI. Alternative 1 - Staff Recommendation

Staff and AIA recommend the Board approve and authorize publication of proposed amendments to Regulation 1618, *United States Government Supply Contracts*, as proposed in Exhibit 2.

A. Description of Alternative 1

Regulation 1618

The proposed amendments to Regulation 1618 include:

- Throughout the regulation - Number previously unnumbered paragraphs to provide points of reference and to comply with regulatory numbering protocol.
- Subdivision (a)(2) - Delete the last sentence to reflect that FAR no longer excludes “special tooling” from the definition of tools, and add an effective date for the inclusion of special tooling in direct consumable supplies.
- Subdivision (a)(3) - Add a statement that the allocation of overhead materials must be consistent with government cost accounting standards.
- Subdivision (b)(2)(A) and (B) - Separate the discussion of the application of tax to supplies into direct consumable supplies and indirect consumable supplies.
- Subdivision (b)(2)(B) - Delete the reference to title passage when indirect consumable supplies are allocated to contracts, some of which are other than government cost reimbursement contracts or fixed price contracts in which title transfers prior to use.
- Subdivision (b)(3) - Add a sunset date for the application of FAR 52.245-17. Following the sunset date, special tooling is included in the definition of direct consumable supplies.

B. Pros of Alternative 1

- Reflects current FAR provisions in the regulation.
- Clarifies tax applications of direct consumable supplies and indirect consumable supplies.

Issue Paper Number 12-001

C. Cons of Alternative 1

None.

D. Statutory or Regulatory Change for Alternative 1

The regulation requires amendment. No statutory change is required.

Operational Impact of Alternative 1

Staff will notify taxpayers of the amended regulation through outreach efforts.

E. Administrative Impact of Alternative 1

1. Cost Impact

The workload associated with publishing the regulation, audit manual, and outreach efforts are considered routine. Any corresponding cost would be absorbed within the Board's existing budget.

2. Revenue Impact

None. See Exhibit 1.

F. Taxpayer/Customer Impact of Alternative 1

None.

G. Critical Time Frames of Alternative 1

Implementation of the regulation will begin 30 days following approval of the regulation by the State Office of Administrative Law.

VII. Other Alternative

A. Description of Alternative 2

Do not amend the regulation.

B. Pros of Alternative 2

None.

C. Cons of Alternative 2

The regulation will not accurately reflect current FAR provisions.

D. Statutory or Regulatory Change for Alternative 2

None.

E. Operational Impact of Alternative 2

None.

Issue Paper Number 12-001

F. Administrative Impact of Alternative 2

1. Cost Impact

None

2. Revenue Impact

None. See Exhibit 1.

G. Taxpayer/Customer Impact of Alternative 2

Regulation will not accurately reflect the current provisions of the FAR.

H. Critical Time Frames of Alternative 2

None

Preparer/Reviewer Information

Prepared by: Tax Policy Division, Sales and Use Tax Department

Current as of: February 28, 2012

REVENUE ESTIMATE

STATE OF CALIFORNIA
BOARD OF EQUALIZATION



Proposed Amendment to Regulation 1618, *United States Government Supply Contracts*

I. Issue

Should Regulation 1618, *United States Government Supply Contracts*, be amended to conform the regulation to changes in the Federal Acquisition Regulation (FAR)?

II. ALTERNATIVE 1 - STAFF RECOMMENDATION

Staff recommends the Board approve and authorize publication of proposed amendments to Regulation 1618 to:

- Address the deletion of FAR 52.245-17, *Special Tooling*,
- Separate for clarity the discussion of the application of tax on purchases of direct consumable supplies and indirect consumable supplies, and
- Update the wording throughout the regulation for clarity.

Mr. Joe Vinatieri and the Aerospace Industries Association (AIA) agree on the proposed amendments. The proposed amendments are attached as Exhibit 2.

III. Other Alternative Considered

Do not amend Regulation 1618.

Background, Methodology, and Assumptions

Alternative 1 – Staff Recommendation

There is nothing in staff recommendation that would impact sales and use tax revenue. Staff recommendation only amends Regulation 1618 to conform to the FAR or Title 48 Code of Federal Regulations (CFR), Part 52. Staff recommendation would:

- Throughout the regulation - Number previously unnumbered paragraphs to provide points of reference and to comply with regulatory numbering protocol.

FORMAL ISSUE PAPER 12-002

- Subdivision (a)(2) - Delete the last sentence to reflect that FAR no longer excludes “special tooling” from the definition of tools, and add an effective date for the inclusion of special tooling in direct consumable supplies.
- Subdivision (a)(3) - Add a statement that the allocation of overhead materials must be consistent with government cost accounting standards.
- Subdivision (b)(2)(A) and (B) - Separate the discussion of the application of tax to supplies into direct consumable supplies and indirect consumable supplies.
- Subdivision (b)(2)(B) - Delete the reference to title passage when indirect consumable supplies are allocated to contracts, some of which are other than government cost reimbursement contracts or fixed price contracts in which title transfers prior to use.
- Subdivision (b)(3) - Add a sunset date for the application of FAR 52.245-17. Following the sunset date, special tooling is included in the definition of direct consumable supplies.

Other Alternatives Considered

Alternative 2 – Do not amend Regulation 1618.

There is nothing in the alternative 2 that would impact on sales and use tax revenue.

Revenue Summary

Alternative 1 – Staff recommendation does not have a revenue impact.

Alternative 2 – Does not have a revenue impact

Preparation

Mr. Bill Benson, Jr., Research and Statistics Section, Legislative and Research Division, prepared this revenue estimate. Mr. Robert Ingenito, Chief, Research and Statistics Section, Legislative and Research Division, and Ms. Susanne Buehler, Chief, Tax Policy Division, Sales and Use Tax Department, reviewed this revenue estimate. For additional information, please contact Mr. Benson at (916) 445-0840.

Current as of March 5, 2012.

Regulation 1618. United States Government Supply Contracts.

Reference: Sections 6007 and 6381, Revenue and Taxation Code.

Aerospace Corp. v. St. Bd. of Equalization (1990) 218 Cal.App.3d 1300.

(a) Definitions.

(1) "United States Government supply contract" means a contract with the United States to furnish, or to fabricate and furnish, tangible personal property including ships, aircraft, ordnance, or equipment, whereby title to tangible personal property purchased for use in fulfilling the contract passes to the United States pursuant to the title provisions contained in the contract before the contractor uses the property to perform the function or act for which the property was designed or manufactured. The term "U.S. Government supply contract" does not include contracts to construct improvements on or to real property or to the purchase of tangible personal property for use in fulfilling such contracts.

(2) "Direct consumable supplies" means supplies, tools, or equipment consumed in the performance of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~"Tools" as used in this definition does not include "special tooling" subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17. Effective June 14, 2007, "Tools" as used in this definition includes "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.~~

(3) "Overhead materials" means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

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(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

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~~(1) 1. Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,~~

~~(2) 2. Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.~~

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in this manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

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BEFORE THE CALIFORNIA STATE BOARD OF EQUALIZATION

450 N STREET

SACRAMENTO, CALIFORNIA

REPORTER'S TRANSCRIPT

MARCH 20, 2012

BUSINESS TAXES COMMITTEE

Reported by: Juli Price Jackson

No. CSR 5214

P R E S E N T

1
2
3
4 For the Board
of Equalization:

Betty T. Yee
Chair

5
6 Michelle Steel
Member

7 Jerome Horton
Member

8
9 George Runner
Member

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

13
14 Diane G. Olson
Chief, Board
Proceedings Division

15
16 For Staff:

Susanne Buehler
Chief, Tax Policy
17 Division, Sales and Use
Tax Department

18 Cary Huxsoll
19 Tax Counsel
Tax and Fee Division
20 Legal Department

21 Kevin Hanks
Chief, Sales and Use Tax
22 Administration/
Headquarters Operations
23 Division, Sales and Use
Tax Department

24
25 Randy Ferris
Acting Chief Counsel
Legal Department

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1 450 N STREET
2 SACRAMENTO, CALIFORNIA
3 MARCH 20, 2012

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5 MS. OLSON: Our next item is Business Taxes
6 Committee. Ms. Yee is the Chair of this Committee.

7 Ms. Yee.

8 MS. YEE: Thank you very much, Ms. Olson.

9 Members, we have three items on the Business
10 Taxes Committee agenda.

11 If I could start out with item 1, proposed
12 amendments to Regulation 1618, relating to the United
13 States government supply contracts. And I'll ask staff
14 to introduce the issue.

15 Good morning.

16 MS. BUEHLER: Good morning. I'm Susanne
17 Beuhler with the Sales and Use Tax Department.

18 We have three agenda items for your
19 consideration this morning. For agenda item 1, Cary
20 Huxsoll from our Legal Department is with me today.

21 Staff requests your approval and authorization
22 to publish proposed amendments to Regulation 1618,
23 United States government supply contracts. The proposed
24 amendments conform the regulation to the US Government
25 Federal Acquisition Regulation, also referred to as FAR.

26 In 2007 several government property clauses in
27 FAR were combined and the specific clause for special
28 tooling was deleted. Staff and interested parties agree

1 to the proposed amendments.

2 We would be happy to answer any questions you
3 may have.

4 MS. YEE: Thank you very much.

5 Good morning.

6 Did you want to say anything else on the issue?

7 MR. HUXSOLL: No.

8 MS. YEE: Okay.

9 MR. HUXSOLL: Sorry about that.

10 MS. YEE: All right, discussion, Members?

11 MR. HORTON: None.

12 MS. YEE: Okay, hearing none is there a motion?

13 MR. HORTON: Move adoption.

14 MS. YEE: Okay. We have a motion by Mr. Horton
15 to adopt the proposed amendments and authorize
16 publication.

17 Yes?

18 Okay, is there a second?

19 MS. MANDEL: Second.

20 MS. YEE: Second by Ms. Mandel. Without
21 objection, such will be the order.

22 Next item is proposed revisions to
23 Sections 901.000 through 906.000 of the Compliance
24 Policy and Procedures Manual, Chapter 9.

25 Ms. Buehler.

26 MS. BUEHLER: For agenda item 2, Mr. Kevin
27 Hanks from the Sales and Use Tax Department is joining
28 us.

1 MS. YEE: Okay. Let me -- before you proceed,
2 we have a couple of speakers on this item. I'll ask
3 them to come forward as the presentation is being made
4 to us.

5 Ms. Sturdivant, Ms. Bouma, and Mr. Myers,
6 please come forward.

7 Mr. Hanks, you want to just do an introduction
8 and then we'll hear from our speakers?

9 Ms. Buehler, sorry.

10 MS. BUEHLER: In agenda item 2, staff requests
11 your approval on proposed revisions to the Compliance
12 Policy and Procedures Manual Chapter 7 -- Chapter 9,
13 excuse me, to incorporate guidelines and procedures
14 related to local and district tax reallocations.

15 Staff and interested parties are in agreement
16 on most procedures as provided in action item 1.
17 However, staff and interested parties disagree on a
18 number of issues, including the requirement that a copy
19 of the contract between the jurisdiction and its
20 representative must be provided before the
21 representative is given access to BOE records; the
22 minimum threshold processing funds transfers, the due
23 dates for the Allocation Group to acknowledge
24 submissions and follow up on aged assignments; the CCPM
25 language and procedures for establishing a date of
26 knowledge; and the appropriate threshold for informing a
27 jurisdiction, as a courtesy, when pending refund or
28 credit in an audit results in a large deallocation.

1 To facilitate the discussion, we proposed that
2 after staff presents an action item, the speakers make
3 their presentation for that item. Staff can then
4 address any questions you may have and ask the Board to
5 vote on that action item before moving on to the next
6 item.

7 MS. YEE: Okay, thank you very much.

8 I -- if there's agreement, I think I would like
9 to take up Ms. Buehler's recommendations, go through
10 action item by action item, if that's appropriate.

11 Okay. So, action 1, looks like we have pretty
12 broad agreement on this?

13 MS. BUEHLER: Right. As agreed to with
14 interested parties, we ask the Board appr -- to approve
15 the rewrite of Sections 901 through 906 of the CCPM.

16 MS. YEE: Okay. Discussion, Members?

17 Okay. I think what I'd like to do is also take
18 action on each of them separately as well. That may
19 be --

20 MS. BUEHLER: That would be great.

21 MS. YEE: -- appropriate to dispense with --

22 MR. HORTON: Okay.

23 MS. MANDEL: What do you mean, each one
24 separately?

25 MS. YEE: Each action item.

26 MS. MANDEL: Oh, yeah, that's what I thought we
27 were doing.

28 MS. YEE: Yeah, okay, good.

1 May I have a motion on action item 1?

2 MR. HORTON: Yes, move approval and
3 authorization to move forward on publication.

4 MS. YEE: Okay. Motion by Mr. Horton, second
5 by Ms. Steel.

6 Without objection, that motion carries.

7 How about action item 2?

8 MS. BUEHLER: In action item 2 the requirement
9 that a designated person provide a copy of its contract
10 with the jurisdiction, we ask the Board approve either
11 staff's recommendation, that a copy of the contract
12 between the representative and the jurisdiction be
13 provided before repre -- the representative is given
14 access to BOE records or MuniServices' recommendation
15 that a designated person is not required to provide a
16 contract before it can access BOE records.

17 MS. YEE: Okay, let me have you stop there.

18 Do we have any testimony on this issue?

19 ---o0o---

20 CHRISTY BOUMA

21 MUNISERVICES

22 ---o0o---

23 MS. BOUMA: Madam Chair, Members, Christy Bouma
24 representing MuniServices.

25 I would just like to make a general comment. I
26 will defer to Mr. Myers on the specificity.

27 Just to thank the Board for their time and all
28 the staff investment on this process. As you know, this

1 was before you probably over a year ago and you sent it
2 to interested parties, which we appreciate, since really
3 -- as I heard earlier this morning all of the discussion
4 about providing good customer service.

5 Under this umbrella the local jurisdictions, on
6 behalf of whom you collect this taxes, are your
7 customers as well as the taxpayers that attempt to
8 comply with the tax laws.

9 So, we appreciate all the time and also the
10 opportunity to comment on these items where we might
11 disagree.

12 MS. YEE: Okay. On this particular action
13 item, any -- yes, Mr. Myers.

14 ---o0o---

15 ERIC MYERS

16 MUNISERVICES

17 ---o0o---

18 MR. MYERS: Thank you, Madam Chair, Members.

19 I think our comment is very simple on this
20 particular item. We have no objection to providing the
21 contract. We've been doing so for years.

22 We just don't think that Section 7056, the
23 statute, requires us to provide that contract before
24 data is allowed to be accessed by consultants on behalf
25 of the cities that have hired them.

26 Beyond that, we don't have a dispute with
27 handing over our contracts, as we've done repeatedly,
28 so --

1 MS. YEE: All right, thank you very much.
2 Discussion, Members, on this particular item?

3 MR. RUNNER: Let me just go back to staff.

4 MS. YEE: Yes.

5 MR. RUNNER: Is this -- again I understand the
6 need and the potential of using contract in order to
7 insure dates of the agreements between the municipality
8 and the -- and the organization that they're dealing
9 with.

10 But the question regards to legislative
11 authority or statute authority, did it require that for
12 information that has been brought up, how do you see
13 that?

14 MR. HUXSOLL: Mr. Runner, it's necessary for
15 the administration of the statute as it's written for
16 staff to be provided a copy of the contract prior to
17 disclosing the records. The Section 7056 requires a
18 person that -- the jurisdiction pass a res -- provide a
19 resolution and that if the person is a -- is not an
20 officer or an employee of the jurisdiction, the
21 resolution must certify that the person has an existing
22 contract with the jurisdiction to examine the records,
23 is required by the contract to disclose information
24 contained or derived from those records only to an
25 officer or an employee of the jurisdiction who is also
26 authorized by the resolution to examine the records, is
27 prohibited by contract from performing consulting
28 services for a retailer during the term of the contract,

1 is prohibited by the contract from retaining information
2 contained in or derived from the records after the
3 contract has expired.

4 So, it's not just necessarily for the
5 resolution, but to have this existing contract. And
6 when staff has been provided these contracts in the past
7 12 months there have been 12 instances of contracts that
8 had either expired or contained clauses contradictory to
9 the limitations in Section 7056.

10 MR. RUNNER: So, you're -- at least what I'm
11 hearing you saying is even though the statute doesn't
12 specifically require the contract, that the
13 requirements within the statute point to the fact that a
14 contract needs to be shown?

15 MR. HUXSOLL: Correct.

16 MR. RUNNER: Okay, thank you.

17 MS. YEE: Thank you, Senator Runner.

18 Comments on this? Further comment?

19 MR. MYERS: No, thank you, Madam Chair.

20 MS. YEE: All right. Do we have a motion?

21 MS. MANDEL: I'll move the staff
22 recommendation.

23 MS. YEE: We have a motion by Ms. Mandel to
24 adopt the staff recommendation, second by Mr. Horton.

25 Without objection, that motion carries.

26 Okay, next section -- next item?

27 MS. BUEHLER: Agenda item 3 is threshold for
28 processing fund transfers.

1 We ask the Board approve either staff's
2 recommendation to set a minimum threshold for processing
3 fund transfers at \$250 per quarter or HdL's
4 recommendation to set the minimum threshold at \$100 per
5 quarter, or MuniServices' recommendation to set the
6 minimum threshold at \$50 per quarter or \$250 for the
7 entire period in dispute, whichever is less.

8 MS. YEE: Okay. Discussion?

9 Do we have testimony on this?

10 ---o0o---

11 ROBIN STURDIVANT

12 THE HdL COMPANIES

13 ---o0o---

14 MS. STURDIVANT: Good morning, Board Members.
15 I'm Robin Sturdivant with The HdL Companies. And we
16 currently represent over 300 local government agencies.

17 And staff is proposing to raise the current
18 threshold, which is \$50, to \$250 a quarter. That
19 represents a 500 percent increase.

20 One of the reasons staff has cited is workload
21 issues and they've described a very arduous process for
22 completing the smaller adjustments. However, during
23 recent BTC Committee meetings to amend Regulation 1807,
24 staff indicated that workload was not an issue and that
25 there was no change needed to the petition process.

26 We'd also like to note that the BOE is in the
27 process of updating their in-house software application.
28 So, we question how much longer the manual process will

1 actually be an issue.

2 And, finally, local government agencies do pay
3 the BOE to administer the local tax program. And these
4 agencies are your clients. And they deserve to receive
5 all the local tax money that's rightfully theirs. We
6 reluctantly agreed of raising the threshold to \$100, but
7 submit that 250 per quarter is excessive. That can add
8 up very quickly. And if a petition takes a year to be
9 resolved, staff's proposal means that that agency will
10 not get \$1,000 in local tax that rightfully belongs to
11 them. And this is money that's already been paid in by
12 the taxpayer and it's just simply gone to the wrong
13 jurisdiction.

14 So, what staff is saying is, we acknowledge the
15 money doesn't belong to that other jurisdiction, but
16 we're just going to let them keep it because our
17 workload won't allow us to put the money in the correct
18 spot.

19 MS. YEE: Okay, thank you very much,
20 Ms. Sturdivant.

21 Mr. Myers?

22 MR. MYERS: Thank you, Madam Chair.

23 We -- we agree in principle, although there is
24 slight differences between our proposal and HdL's. We
25 agree in principle that what we need to do here is look
26 at the benefit to -- to the cities that are paying for
27 administration.

28 So, we're open to changing our position, which

1 has been no increase at \$50 with a \$250 cumulative cap
2 or threshold. We'd be willing to move to the \$100 and
3 the 250 cumulative, if that helps.

4 But we think the principle is what is important
5 here and that is that you have cities who are paying for
6 administration who are now being told, .

7 "You have to meet 250 a quarter in order
8 for us to look at your correction and get you
9 the money."

10 And we think that that shouldn't be the case.

11 MS. YEE: Okay, thank you very much.

12 Discussion, Members?

13 MS. MANDEL: Yeah --

14 MS. YEE: Ms. Mandel.

15 MS. MANDEL: -- I had some questions.

16 MS. YEE: Yes, please.

17 MS. MANDEL: At first when I heard about this
18 issue I was kind of focused on the -- it doesn't take
19 much once you've figured out that the money should have
20 gone to Jurisdiction A instead of Jurisdiction B, that
21 it doesn't take much to do that.

22 And then as I read the paper, I realized, well,
23 that's not really what it's about. What it's about
24 is -- as I take it from the paper, tell me if this is
25 wrong -- is that unless -- unless the petition coming in
26 is at a 250 per quarter threshold, the petition won't be
27 worked at all. So, you wouldn't even get to the point
28 where you figure out, "Oh, yeah, it should have gone to

1 Jurisdiction A instead of Jurisdiction B."

2 It's just that workload -- it's like a
3 threshold for filing a petition, is that correct, the
4 way that you got it set up in the staff recommendation?

5 MR. HANKS: Ms. Mandel, our recommendation
6 is -- is for a \$250 per quarter threshold. And, so, if
7 there is a deallocation that's recommended for \$250,
8 then those are the amounts that we're proposing be
9 reallocated. Even if we've got amounts -- now, if we've
10 got amounts below that, let's -- let's say that we've
11 got ten different -- ten different allocations of the
12 \$250. We've got a deallocation from one jurisdiction
13 and we've got a reallocation to ten other jurisdictions.

14 What we're proposing is that we would still
15 make that adjustment, because the one deallocation
16 totals \$250.

17 MS. MANDEL: Okay. So, let me repeat this
18 because I always want to make sure I understand what
19 you're saying.

20 So, if a petition -- and I'm not familiar with
21 the petitions, I never did that kind of work -- so, if a
22 petition comes in from a jurisdiction that impacts ten
23 other jurisdictions, what you're saying is if one of
24 those ten has -- has a reallocation, deallocation that's
25 at or above the 250 threshold, then the other nine will
26 get it too, because it's --

27 MR. HANKS: Correct.

28 MS. MANDEL: -- right?

1 MR. HANKS: Correct.

2 MS. MANDEL: But -- and -- but -- maybe the
3 consultants can help me out a little bit because here's
4 where I was going with that is I was -- I don't really
5 see -- I don't see an explanation of the workload impact
6 from -- they're willing to go now \$100 from the 50 and I
7 don't really see an analysis of the workload impact from
8 \$100 to \$250.

9 And I kind of thought -- well, what I was
10 hearing at first was how hard is it -- now that you've
11 figured out that somebody's supposed to get the money,
12 how hard is it really to move the money? How much does
13 that really cost?

14 And that's why I -- in reading it again, I
15 thought, well, maybe what staff's saying is
16 jurisdictions don't even file with us 'cause they're not
17 all -- they're not all -- I mean, the one you're talking
18 about is on the back end. I'm a jurisdiction and I want
19 to get three grand and it impacts a bunch of other
20 places.

21 But it may be that a jurisdiction files because
22 they want to get -- and the jurisdictions have said this
23 makes a difference to them -- that they want to get
24 their \$100 a quarter. Maybe it's worth it to them at
25 \$100 a quarter to say,

26 "Hey, they paid it to the guy -- the co --
27 the jurisdiction next door to me and it should
28 have come to me and I want my \$100 a quarter,

1 because over the life of that business being
2 there, \$100 a quarter is going to add up to a
3 lot to me. But my petition right now is only
4 for, you know, a few quarters. But once you
5 figure out that they should have been sending
6 it to me, you know, it's going to be a while."
7 And what I took then when I read the paper
8 again, trying to figure out about how bad is this
9 workload impact, that what was being said was if that
10 jurisdiction comes in, staff's not going to look at the
11 petition.

12 But I don't have a handle on whether that's the
13 case or, you know, how much -- you know, what is it that
14 we're really talking about in terms of -- of the
15 workload that wouldn't have to be done?

16 I can't get -- I couldn't gather that really
17 from the issue paper to see where -- where the dispute
18 lies.

19 And then that gets to the second point that I
20 can follow up with, which was the question about, you
21 know, who's -- who's really paying for the service
22 anyway? And I know we've had a little bit of that
23 discussion before, but can you help me out with --

24 MR. HANKS: Absolutely, absolutely.

25 Ms. Mandel, some of the comments that we wanted
26 to share with the Board Members is -- is we're -- we're
27 mindful of the -- of the cost of the locals to
28 administer this program.

1 And ultimately what we're wanting to do is to
2 provide efficient operations to them for the service
3 that we're providing them for the reimbursements that
4 we're collecting from the local jurisdictions.

5 What -- what we're here to talk about are those
6 efficient operations. What we've analyzed and been able
7 to determine is that approximately 15 to 20 percent of
8 the cases, petitions that we're working in our
9 Allocation Group, relate to these lower dollar threshold
10 amounts, so, \$250 and below. So, approximately 20
11 percent of that workload relates to -- to working
12 these -- these smaller assignments.

13 MS. MANDEL: And -- but let me just interrupt
14 you for a second.

15 But you -- you don't know what -- do you know
16 what it is between the 100 that they're willing to go to
17 and 250? Do we know where it is or we don't yet?

18 MR. HANKS: I don't know the -- the difference
19 between --

20 MS. MANDEL: Okay.

21 MR. HANKS: -- that interval, but I know below
22 \$250 we've got approximately 20 percent of the petitions
23 that -- that we're working in that category.

24 Now what we're mindful of is that there is an
25 opportunity cost to preparing these -- the work
26 associated with these reallocations. And to -- in the
27 sense that we reallocate resources to adopt these
28 reallocations, we're going to be pulling audit resources

1 or outreach resources or collection resources from other
2 parts of the Board's agency.

3 Now to do that equates to an opportunity cost
4 to the locals and to the State of approximately \$350 an
5 hour for each and every hour that these individuals are
6 performing the reallocation work. The State and the
7 locals are not driving that \$350 per hour tax change.

8 Now we're mindful too in reallocating the local
9 tax that we're talking about, there is no net increase,
10 of course, with the local tax to any jurisdiction, apart
11 from a shift of that local tax from one jurisdiction to
12 the next, let's say, from Sacramento to -- to West
13 Sacramento. There's -- it's a zero sum proposition
14 where you're just transferring those local funds.

15 So, we're mindful that -- that being efficient
16 in our operations that the opportunity cost to do this
17 type of workload impacts the locals indirectly in the
18 sense that we don't have collectors working these
19 assignments, collecting accounts receivables, we don't
20 have auditors conducting audits and bringing in that --
21 that level of revenue to the State and to the locals.

22 Also we're mindful that -- that if we do an
23 audit of a taxpayer's business and develop a \$500
24 deficiency in that audit, generally speaking, we don't
25 bill that because it's -- it's not efficient for us to
26 even bill at the \$500 level.

27 Here we're talking a level -- a threshold level
28 that's half of that, \$250. We're proposing that the

1 threshold be raised from \$50 to \$250, although,
2 arguably, one could say that \$500 even might be a more
3 reasonable level from the sense that we don't even bill
4 these types of audits unless we have tax differences of
5 at least \$500 an hour.

6 Now the other rationale, however, for
7 establishing a \$250 threshold is in the audits that
8 we're currently conducting, for any local tax
9 reallocation recommendations we make within our audits,
10 we don't make those reallocations unless we're at the
11 \$250 threshold, which is equivalent to the threshold
12 that we're proposing to the Board Members today.

13 And that's -- that's really the basis for our
14 recommending the \$250 threshold, because it keeps it in
15 sync with what -- the threshold we're using when we
16 conduct our regular audits.

17 And also we're mindful of the opportunity cost
18 of directing more resources towards this reallocation
19 would ultimately cost the locals, not only in staff time
20 to produce the reallocation recommendations, that --
21 that is costing the locals many dollars a year to
22 perform, but also they're not gaining any local tax in
23 the sense that we're shifting local tax from one
24 jurisdiction to the next.

25 Also it's been mentioned that some of the
26 cities would be negatively impacted if they weren't
27 receiving \$50. We've looked at some of the Northern
28 California cities that are quite small, with small

1 populations and receiving only \$29,000 in sales tax
2 revenue. \$50 reduction to that city is -- is really
3 immaterial in terms of an adjustment to even a small
4 city in California, much less a larger city and a larger
5 metropolitan area.

6 Also we're mindful that -- in the sense that
7 we're working reallocations for one city where they're
8 going to derive an increase of \$50. For another case
9 that we're working perhaps that \$50 is removed from them
10 and placed in an -- in another jurisdiction.

11 So, you've got the monies coming to and from
12 each of these local jurisdictions. So, in the sense
13 that they're receiving \$50, well, they might be losing
14 \$50 in the next period when we find a reallocation that
15 is necessary for a subsequent period.

16 So, again, what we're finding is that these --
17 these small, small adjustments that -- that we're
18 working currently at the \$50 threshold, or anything
19 between \$50 and \$250, is requiring significant staff
20 resources to -- to manage that workload. We think would
21 be better spent by using those same resources, working
22 the cases that are \$250 and higher, because ultimately
23 the jurisdictions are going to benefit from -- from more
24 of those higher dollar shifts of local tax money from
25 one jurisdiction to the next.

26 MS. MANDEL: Okay. On the costs, we had this
27 the discussion, I think, a while ago, maybe it wasn't in
28 terms with the reg, I don't remember when it was, about

1 how the costs are figured.

2 'Cause for the local jurisdictions it's kind of
3 a funny thing because the costs -- the costs are paid on
4 an aggregate basis because it's kind of off the top of
5 something, of what's -- I guess, I don't even remember
6 any more -- but I think it's like on an aggregate basis,
7 whereas on the petition side they're looking at it on
8 a -- on a, you know, a single basis of the -- of the --
9 the tax revenue.

10 But as I remember the cost discussion it was
11 that the costs that are allocated is a share of the
12 entire cost of SUTD. Is that how it's done? Because
13 every little thing that SUTD does impacts how many
14 dollars overall come in the door.

15 MR. HANKS: That's correct.

16 MS. MANDEL: So, it's not like there's a
17 separate costing of the petition process, which, you
18 know, at one level the entire petition process benefits
19 only the local jurisdictions and if you could but
20 segregate it out, perhaps their overall costs would
21 actually go up, I don't know.

22 But that that -- that's -- that's the cost
23 methodology, is that --

24 MR. HANKS: Correct.

25 MS. MANDEL: -- right?

26 MR. HANKS: Correct. There's a complex
27 calculation that's -- that's actually described in our
28 Revenue and Taxation Code that goes into the

1 mathematical analysis for calculating that cost. And
2 it's dependent on -- on various factors. Of course, the
3 primary one being the -- the amounts of dollars that
4 are -- that are given to each of the jurisdictions.

5 MS. MANDEL: Okay. And -- and part of why I'm
6 asking these questions is because the impression I had
7 from hearing what the local jurisdictions were concerned
8 about and I would just note, in my every detail queen
9 manner, that in the issue paper when staff states the
10 opposition for this item and they list the cities of
11 San Joaquin and San Diego, actually, the San Joaquin
12 opposition was the San Joaquin Council of Governments,
13 which lists a lot of member agencies and San Diego
14 opposition actually came in from -- and San Joaquin also
15 was for the -- on behalf of the San Joaquin County
16 Transportation Authority and the San Diego reference is
17 to the San Diego Association of Governments, which sent
18 an e-mail, and that, of course, also includes a lot of
19 -- I think it's like 18 cities and the County of
20 San Diego. So, for people who are reading fast and just
21 looking at the issue paper, you know, given all of the
22 time we should at least, you know -- I know you attached
23 the letters and you could look at them and see it was
24 really something else, but just -- if you can just watch
25 that kind of stuff in the future?

26 I didn't have the impression that this entire,
27 you know, cost discussion analysis -- maybe it was --
28 maybe I missed the interested parties meetings, but I

1 couldn't -- like I said, I couldn't get it from the
2 issue paper. And what I was kind of hearing and getting
3 the impression of is, you know, it's our money and we
4 pay for this, and, so, we -- we're willing to go to 100,
5 but, you know, we've -- I got the impression that they
6 may have been -- maybe they just -- I got the impression
7 they were a little bit confused about it the way I was
8 confused about it.

9 Is this -- I don't know if this discussion
10 helps clarify that for them?

11 MS. YEE: Mr. Myers.

12 MR. MYERS: Thank you, Madam Chair.

13 We remain a little bit confused. The argument
14 seems to be that there is an opportunity cost. But we
15 recall that during the discussions on the changes to
16 Regulation 1807, when we were discussing the backlog
17 that the position of staff was they had enough staff to
18 handle the backlog.

19 Yet we're hearing here today that there's an
20 opportunity cost from auditors, who are not the people
21 working our petitions. So, I still remain confused.

22 Our original recommendation was to pull this
23 item off and handle it separately. And we'd be happy
24 with that as well. So, we have a chance to talk through
25 some more with staff, we have a good working
26 relationship with staff. We've been able to come to
27 some agreements on some other items.

28 As of yet, however -- excuse my voice -- as of

1 yet, we haven't heard an explanation as to why this is a
2 necessary step, given the background that I just
3 mentioned. So --

4 MS. YEE: Thank you, Mr. Myers.

5 Miss Sturdivant.

6 MS. STURDIVANT: To address Ms. Mandel's point,
7 HdL represents over 300 hundred local government
8 agencies who oppose this.

9 And I understand that Mr. Hanks feels that the
10 \$50 a quarter is immaterial to a smaller city. That's
11 his opinion and I respectfully disagree with that.

12 Some of the smaller cities are usually the ones
13 that have the smaller taxpayers. And they are usually
14 the ones that the smaller petitions will directly
15 affect. In those smaller cities, in this economic
16 climate, every single dollar counts, whether it's 50,
17 whether it's 250, it -- it all matters.

18 And again I'd like staff, if they could, to
19 address if this will continue to be an issue after
20 the -- your in-house software application is updated?
21 Because they talk about this is a manual process. And
22 I'm assuming that once the software rewrite's complete
23 that that will no longer be the case. So, I'd like them
24 to talk about and what the time frame is --

25 MS. YEE: Yeah.

26 MS. STURDIVANT: -- as far as that's concerned.

27 MS. YEE: That was my question as to whether
28 that will make things improve.

1 MR. HANKS: I agree with Miss Sturdivant. I
2 believe that with the adoption of CROS we're certainly
3 going to be in -- in the arena where we're going to be
4 able to have a more automated process in calculating the
5 reallocations.

6 One of the subjects that we're going to talk
7 about in a few minutes, I think, is -- relates to
8 notification. And that's -- that's a very difficult
9 process for us to compute because IRIS simply doesn't
10 give us the information that -- that we can use to
11 readily determine if -- if a deallocation meets a
12 certain threshold. So, it's quite labor intensive for
13 us to do these calculations.

14 I think in the future, with the adoption of
15 CROS we will have more automated processes and queries
16 that we can use to assist us in facilitating these --
17 these adjustments electronically rather than manually.

18 MS. YEE: Have you provided input to be sure
19 that capacity will be there?

20 MR. HANKS: We are discussing that, yes.

21 MS. YEE: All right.

22 MR. HANKS: Yes.

23 MS. YEE: Okay. I -- I want to jump in a bit
24 because I -- and I appreciate the dialogue that
25 Ms. Mandel and Mr. Hanks, you had.

26 I guess I'm troubled by the fundamental issue
27 here and that is really, you know, workload
28 considerations certainly on our minds if that, in fact,

1 is what is driving this particular change, but we have a
2 responsibility to be sure that jurisdictions receive the
3 right allocation of tax proceeds and -- that they are
4 otherwise entitled to receive. And what I need to see
5 happen is we adopt the change here that could be
6 facilitated in resolving, once we get CROS up and
7 running.

8 And I agree with Ms. Sturdivant, I mean, small
9 jurisdictions are just really hungry for dollars right
10 now and there's very little that they can do. This is
11 the one avenue and it -- and it could make a difference
12 in terms of some of the things that they are able to
13 fund or not fund.

14 But it just seems to me that if this is a
15 workload issue, if we kept the current threshold, it's
16 either going to be we keep the current threshold and all
17 of this takes more time or we change the threshold and
18 it becomes a little bit more efficient in terms of how
19 these petitions get processed.

20 MR. HANKS: Correct.

21 MS. YEE: Okay.

22 MR. HANKS: Correct.

23 MS. YEE: So, it's a tradeoff.

24 But, I mean, there was a little hope with CROS
25 on the horizon, so, that -- that's sometime out.

26 MR. HANKS: It is.

27 MS. YEE: But -- but I'm troubled by kind of
28 losing sight a little bit about our responsibility to be

1 sure that we are trying to arrive at the right
2 allocation of tax.

3 I understand this is a zero sum game and that
4 our costs aren't fully recovered with respect to what
5 local jurisdictions are -- are paying us, but I just
6 don't want us to lose sight of that. I think we have a
7 fundamental responsibility in that regard. So --

8 MR. HANKS: We wholly agree.

9 MS. YEE: -- it's a balancing act.

10 MR. HANKS: We wholly agree.

11 MS. YEE: Senator Runner and then Mr. Horton,
12 I'm sorry.

13 MR. RUNNER: Yeah, just real quick. I am not
14 persuaded with this new amount. I'm -- let me just tell
15 you a couple of my observations.

16 One is, Mr. Hanks, the analogy is not a good
17 one when we say, "Gee, we don't -- we don't go and
18 collect anything less than \$500 because of the cost."

19 There's a difference. No. 1, we're the State
20 dealing with the State's money. Here we're dealing with
21 somebody else's money. And to me this would be, you
22 know, like a bank deciding to write off a cost because
23 the bank wants to -- because it's going to cost them too
24 much to go do something. But I don't want the bank
25 writing off any of my money because it cost the bank too
26 much time. So, I think that's -- I have difficulty with
27 the idea that the threshold amount, you know, and what
28 we choose to do, to chase after an amount of money.

1 The other issue is we're talking about \$250 a
2 quarter. Some of these disputes are more multiple
3 quarters, correct?

4 I mean, they might have an audit that might
5 be -- I don't know, could they be two years long?

6 MR. HANKS: Senator --

7 MR. RUNNER: And so now you're talking about --
8 now you're talking about not \$250, but you're talking
9 about what could be just a shade under \$2,000.

10 MR. HANKS: Yeah.

11 MR. RUNNER: And I can tell you I represent a
12 lot of those little communities and, yes, \$2,000 makes a
13 big difference to them.

14 So, I guess my concern is -- I actually
15 wouldn't have much -- as much trouble with this if it
16 was a cumulative \$250 as much as I have concerns with it
17 being \$250 per quarter, which then could amount to a
18 much larger amount of dollars.

19 The other issue is, I guess I'm not convinced
20 of, and that is we're talking about workload and
21 efficiencies and -- and I guess if I'm the customer,
22 like these folks are -- then I need to hear from you
23 what you're going to get me then with these
24 efficiencies. If you're going to make it faster and
25 efficient, what are my -- what am I going to get? What
26 are my municipalities going to get?

27 MR. HANKS: Right.

28 MR. RUNNER: What's going to happen? What's

1 going to be the benefit from -- that they're going to
2 receive as a result of the fact that we're going to go
3 ahead and set this new higher limit?

4 MR. HANKS: Right. I think that's a great
5 question, Senator Runner. And I'd be happy to explain
6 that that I think what the locals are going to derive is
7 they're going to drive a shorter petition period in
8 which we've got time to make recommendations to grant
9 the reallocations that are necessary.

10 Believe me, we're 100 percent in agreement
11 with -- with everyone --

12 MR. RUNNER: Can I stop you right there real
13 quick?

14 'Cause I was here at the hearing where we said
15 we had enough staff, that we did not have a staff
16 problem with driving petition issues.

17 I mean, I thought we -- I thought -- because we
18 talked about that, we talked about do we need to put
19 more people on it. And we said, no, we don't.

20 And, so, I guess I'm struggling now with what
21 we talked about a few months ago versus what we're
22 talking about today.

23 MR. HANKS: Right. And I'm looking at our
24 inventory of petitions. As you know the petitions come
25 in and they're worked as they come in. I think at the
26 last meeting that we had, we had a petition inventory
27 that was rising and approximately 5,000. Back in
28 September of 2011, actually, that number was as low as

1 4600. Since then, however, the number of petition
2 inventory has increased to 5400 and that's as of January
3 of '12.

4 So, we're mindful that we are actually
5 receiving an increased level of petitions. That volume
6 somewhat fluctuates over time, but --

7 MR. RUNNER: And of that -- just to clarify
8 from what you had said earlier -- and of that 5400, we
9 said 15 to 20 percent of those are less than \$250?

10 MR. HANKS: That's correct.

11 MR. RUNNER: Per quarter?

12 MR. HANKS: Per quarter.

13 MR. RUNNER: Not the -- not an aggregate amount
14 over time, but per quarter?

15 MR. HANKS: Per quarter, that's correct.

16 MR. RUNNER: Could some of those be, like,
17 lengthy, like two or three years in dispute?

18 MS. MANDEL: Meaning the length of the
19 petition --

20 MR. RUNNER: Length of the petition --

21 MS. MANDEL: -- from date of knowledge?

22 MR. HANKS: Oh, absolutely, absolutely.

23 MR. RUNNER: So --

24 MR. HANKS: That includes all of our petition
25 inventory.

26 MR. RUNNER: So, you could be talking about
27 several thousand dollars to a local community?

28 MR. HANKS: We could, we could. And -- and I

1 think what we're attempting to do is the shorten that
2 petition period so that -- that we're able to -- to
3 effectively manage that increased workload as it comes
4 in, but process the reallocations in a shorter period of
5 time so that the locals get the advantage of those
6 reallocations sooner rather than later.

7 MR. RUNNER: Okay.

8 MR. HANKS: I think that's -- that's our
9 ultimate goal here. And I think increasing the
10 threshold to the \$250 level would -- would achieve that.

11 MR. RUNNER: I guess -- the bottom line of this
12 is I guess we haven't sold the customer that they're
13 going to get a benefit from this yet, have we?

14 MR. HANKS: Correct.

15 MR. RUNNER: Thanks.

16 MR. HANKS: That's correct.

17 MR. HORTON: Madam Chair?

18 MS. YEE: Mr. Horton, please.

19 MR. HORTON: Question of the Department, is it
20 possible to -- to determine what the cost is attributed
21 to the reallocation process?

22 MR. HANKS: Yes. Actually, just in looking at
23 our Allocation Group and in connection with the
24 petitions that -- that they're working, the -- the total
25 cost for that effort is approximately a million dollars
26 a year -- just -- just for Allocation Group staff and
27 handling and processing this petition workload.

28 MS. MANDEL: That doesn't include Appeals, it's

1 just the Allocation Group, right?

2 MR. HANKS: Correct. That includes just that
3 group, it doesn't include our Local Revenue Section.

4 And as Ms. Mandel had indicated, there's a -- a
5 rather complex formula, actually, that accounts for the
6 reimbursement charges that -- that are made to the
7 locals. And it really encapsulates some of the work
8 that all of us are involved in because to a certain
9 extent, all of our work touches on the locals as well.

10 MR. HORTON: And, so, as the administrative
11 body, how is the Board -- is there indication that the
12 taxpayer actually pays for the service? How is that
13 accomplished?

14 MR. HANKS: Through reimbursements.

15 And, so, reimbursements are paid to the -- to
16 the Board or are adjusted through our budget section. I
17 am not sure of the detailed mechanics of that, but --

18 MR. HORTON: Are these general reimbursements
19 or reimbursements specific to the allocation process or
20 deallocation process?

21 MR. HANKS: I don't know that. I would have to
22 talk someone from -- from budgets. I'd be happy to look
23 into that for the Members.

24 MR. HORTON: The \$50, \$100, \$250, I think that
25 the concern for me is is that a \$50 transaction can
26 actually amount to a \$1,000 transaction if it's never
27 corrected. The company could grow. They could
28 purchase -- there could be transactions that take place

1 that causes the tax allocation to increase. And, so,
2 it's not just the \$50 allocation that would concern me.
3 And there's a larger exposure to -- to the cities
4 because it's unknown as to what the ultimate exposure
5 will be to the city.

6 The question is, there -- is there a need to
7 correct the problem? And the answer should be yes, as
8 long as the funding is there allow the Board of
9 Equalization to accomplish that objective, we should
10 correct it because it's unknown what the allocation may
11 ultimately be.

12 We may conduct an audit and find in that audit
13 process that there is an additional liability that
14 actually reveals that it's far more than \$50 that we're
15 looking at as far as the ultimate allocation.

16 My concern goes to the taxpayer. What is the
17 cost -- and this is a question of the consultants --
18 what is the cost of the taxpayer putting forth a
19 reallocation and deallocation at a \$250, \$50 rate,
20 presuming that that's constant, that that stays the
21 same?

22 I mean I put forth the potential possibility
23 that it's the unknown and it could be more, but if they
24 go into saying,

25 "We see that there is a \$50 problem here
26 that we need to correct, cities, in order for
27 you to pay us, the consultants, and for you to
28 accumulate this and do the work necessary in

1 order to justify this internally, it's going to
2 cost you X."

3 Any numbers in that regard?

4 MR. MYERS: Let me make sure I understand the
5 question first.

6 So, you're asking what the cost is for the
7 city?

8 MR. HORTON: In order --

9 MR. MYERS: What we would charge the city to
10 submit?

11 MR. HORTON: I'm not -- I'm not asking you to
12 disclose what you would charge to submit.

13 MR. MYERS: Okay.

14 MR. HORTON: But I'm asking you to give me an
15 estimate as what the cost is attributed to the city, the
16 work that the city has to do, the work that you're doing
17 and so forth. And I'm trying to understand the
18 materiality of this as we look at costs.

19 There's a cost for the Board; there's a cost
20 for the city. I personally think that if there's an
21 error, we should correct it, as long as we have the work
22 force in order to accomplish that objective,
23 irrespective of the threshold. But I am concerned about
24 the materiality of this as it relates to the taxpayer.

25 MR. MYERS: Fair enough.

26 So, I would say two two things. No. 1, it is
27 no secret, certainly a matter of public record, that we
28 -- we're paid a contingency fee. So, there is no fixed

1 charge to the city for us to submit a small claim versus
2 a large claim.

3 However, in order for us to determine there's a
4 claim, there's always a level of work we have to do.
5 And that's true, I think, for the Department as well.

6 Unless this is going to be threshold that's
7 says it's not -- "It doesn't say, "250 in this box,
8 throw it out," they have to look at it as well and say,

9 "Well, is there a misallocation here in the
10 first place? How much is it going to be? How
11 many quarters are at issue here?"

12 We have to look at all of those. I would say
13 that the lower -- the lower the amount, the more likely
14 it is -- it's a -- that it's not a complicated error,
15 but that's not always true. You can get complicated
16 errors that take a lot of work on of our side to
17 investigate, a lot of work on the Department's side to
18 investigate at a low threshold.

19 So, you know, I would say that our proxy
20 measure would be complexity as opposed to number of
21 dollars, but they do follow somewhat roughly.

22 And I'll let Ms. Sturdivant comment as well.

23 MS. STURDIVANT: I would agree with Eric --
24 Eric's assessment.

25 And I'd also like to point out that, you know,
26 to a larger city \$50 or \$250, you know, if their local
27 tax revenue is several million a quarter, that's not a
28 lot. But again to a smaller city, where their local tax

1 revenue is maybe \$30,000 a quarter, that small petition
2 becomes that much more valuable.

3 You know, and it doesn't -- based on how our
4 contracts work with the city, they're not actually
5 putting any time in themselves prior to submitting the
6 petition. That's something that the consultant does.

7 And, again, as Eric said, the time varies,
8 depending on what type of misallocation it is, how much
9 research goes into it on our part.

10 But the bottom line is is that money belongs to
11 that city. Unfortunately, it went to the other city
12 and, basically, what staff's saying is it's too much
13 work for us, so, we're just going to let that other city
14 keep your money. And that's not right, that's not what
15 the cities pay for.

16 MR. HORTON: Okay.

17 MR. HANKS: If I could add one -- one comment
18 to this --

19 MS. YEE: Mr. Hanks.

20 MR. HANKS: -- Mr. Chairman?

21 I wanted to note that any tax area code changes
22 that -- that are being recommended, certainly those are
23 being processed no matter what -- what threshold is --
24 is identified.

25 So, if -- if there's new information that --
26 that is supplied to the Board that indicates that the
27 allocation should be made going into the future
28 prospectively from a new jurisdiction, certainly

1 those -- those changes are processed, irrespective of
2 any -- any threshold level.

3 MR. HORTON: Okay.

4 MR. HANKS: So, it's not accurate that we're
5 not going to make adjustments and just cast aside
6 everything that --

7 MR. HORTON: So, we'll --

8 MR. HANKS: -- doesn't meet the \$250 threshold.

9 MR. HORTON: -- so, we'll make those adjustment
10 irrespective?

11 MR. HANKS: Absolutely.

12 MR. HORTON: Okay.

13 MR. HANKS: Absolutely.

14 MS. MANDEL: So, the threshold's not a
15 threshold for them to file a petition, the thresh --
16 you'll still -- they'll take -- you'll take petitions at
17 that lower amount because it might impact a future
18 change? You'll work the petition?

19 MR. HANKS: Correct, if it --

20 MS. MANDEL: And it's just when you go, "Aha,
21 this -- they were right," you're only going to make the
22 change at these lower numbers and assuming nobody
23 involved in the petition gets hit for 250 or more,
24 you're just -- you're going to make the adjustment for
25 the future just not for the past?

26 MR. HANKS: Correct, correct.

27 MS. MANDEL: And --

28 MR. HANKS: Within the time period --

1 MS. MANDEL: Okay. That gets to the --

2 MR. HANKS: -- specified.

3 MS. MANDEL: -- that gets a little bit to the
4 -- Mr. Runner's, you haven't sold the customer because
5 that's where it's hard to understand the workload
6 element of it and then -- and then, you know, CROS comes
7 in and we're okay.

8 And there've been some changes since the
9 discussion on the petition reg within this group and
10 personnel and all kinds of things that have been going
11 on in our world at BOE and whether there is
12 efficiencies -- I mean, I -- I know you said that it's
13 very complicated.

14 They just see it as, you know, one more tiny
15 step for man. So, I'm just not -- and because I don't
16 know the answer, really, except that I hear you say,
17 "Oh, it takes a lot."

18 I -- I'm not too -- I'm at a disjoint and not
19 that comfortable, knowing -- because if we say no now
20 and then it gets better later, you know, is there no
21 going back? You know, do we all forget about it and
22 it's just at this and we're never going to -- anyway,
23 I'm sorry, I just --

24 MR. HORTON: That's okay.

25 MS. MANDEL: -- I feel discombobulated, I
26 guess, on where to be, really.

27 MS. YEE: Mr. Horton.

28 MR. HORTON: Yeah, it's a little -- it's a

1 little confusing. Why are we even having the
2 conversation?

3 I would think that the consultants would not
4 submit a petition that -- without giving some
5 consideration to the cost benefit to their clients as
6 well as to themselves. And, so, at \$50 you're talking
7 -- if it's -- if it's a six-month adjustment, \$300, a
8 year -- do you see where I'm going?

9 Sounds like if it's complex, even at \$50 the
10 complexity is insignificant, I mean it's -- it's not the
11 measurement. The complexity can be there for a \$50 a
12 month allocation as well as a \$500 a month allocation.
13 It can be equally complex.

14 And the representatives are the ones in the
15 position to sort of make that determination. And it
16 seems to me that capitalism would sort of dictate the
17 work. In addition -- I mean I certainly appreciate the
18 sense of just getting it right, which is -- which is my
19 position at any time and than you for the service and
20 providing us the information so that we can get it
21 right.

22 But in measuring workload cost, benefit,
23 efficiencies and effectiveness is what we all sort of do
24 and maybe we ought to give this some time and kind of
25 figure that out so that there can be a true discussion
26 about, "Here's what the cost is to the State Board of
27 Equalization." It's been alluded to that that's a
28 million dollars, which is immaterial, necessarily, to

1 the customer, other than the fact of the opportunity
2 costs he made reference to, that that's a million
3 dollars worth of service that is no longer available
4 to -- to the constituents.

5 But if we spend a million dollars to make a
6 \$200,000 adjustment, you know, there is some --
7 some fiduciary responsibility concerns there as well.

8 And if the taxpayer is -- is spending -- as far
9 as their opportune time, their City Manager, their
10 Controller and so forth, to the extent that they're
11 participating, if that cost is in excess of \$500 to make
12 a \$250 adjustment, there might be some concern on both
13 ends.

14 So, it seems to me that we have a commonality
15 in trying to get to where this threshold number is
16 beneficial to all parties involved. And I don't -- and
17 I don't necessarily hear that we have gotten there.

18 Okay, Madam Chair.

19 MS. YEE: Thank you very much.

20 MR. RUNNER: In light of a long agenda, I'd
21 like to make a motion that --

22 MS. YEE: Please.

23 MR. RUNNER: -- we put this over for further
24 review, this particular item.

25 MS. YEE: Okay.

26 MS. STEEL: I'll second that.

27 MS. YEE: Motion by Mr. Runner to put over
28 action item 3 for further review, second by Ms. Mandel.

1 Without objection, Members?

2 Such will be the order, thank you.

3 Okay, Ms. Buehler, next item?

4 MS. BUEHLER: Action item 4 is the time frame
5 to acknowledge submissions. We ask the Board approve
6 either staff's recommendation to allow 30 calendar days
7 for the Allocation Group staff to acknowledge the
8 missions intended as petitions or MuniServices'
9 recommendation to allow 7 calendar days.

10 MS. YEE: Okay. Do we have testimony on this
11 item?

12 MS. BOUMA: Madam Chair, Members, Christy,
13 MuniServices.

14 We would like to let the record stand on this
15 issue. We have no further comment.

16 MS. YEE: Okay, thank you. Discussion,
17 Members?

18 MS. MANDEL: Yeah.

19 MS. YEE: Ms. Mandel, please.

20 MS. MANDEL: Questions on this one.

21 Okay. This is sort both the time frame pieces
22 together; is that right? Or is this just one of the --
23 wait a minute, let me get to the right place.

24 Oh, this is just the acknowledgement.

25 No, I don't have an issue with the
26 acknowledgement.

27 MS. YEE: Okay, very well.

28 Other discussion an action item 4?

1 MR. RUNNER: Move action item 4.

2 MS. YEE: Okay.

3 MR. HORTON: Second.

4 MS. YEE: Motion by Mr. Runner, second by
5 Mr. Horton.

6 Without objection, that motion carries.

7 Next item, action item 5, Ms. Buehler?

8 MS. BUEUHLER: Action item 5 is documenting a
9 date of knowledge. We ask the Board approve either
10 staff proposed explanation of when a date of knowledge
11 is operationally documented by BOE staff or
12 MuniServices' proposed language, which provides that
13 when establishing a date of knowledge, staff must
14 include the information required under Regulation 1807
15 that supports the probability of a misall --
16 misallocation and should contact the taxpayer to
17 establish that there is a basis for questioning the
18 reported allocation unless circumstances do not warrant
19 contact.

20 MS. YEE: Okay. Testimony on this item?

21 MR. MYERS: Yes, Madam Chair.

22 MS. YEE: Mr. Myers.

23 MR. MYERS: Our -- I'll take the responsibility
24 here for maybe muddying the waters. Our basic point is
25 simply this, we all agree that there should be
26 sufficient facts, whether it's a operationally
27 documented date of knowledge or a petition. But there
28 should be sufficient factual information to support the

1 probability of a misallocation. The question is, what
2 does that mean?

3 We thought that a simple way to answer that
4 question would be to say, "Well, it means what we said
5 it meant in Regulation 1807."

6 We think staff has raised a legitimate concern
7 about having to contact -- excuse me, about having to
8 contact the taxpayer in every case. We submit it's in
9 language suggesting that it wasn't necessary. We are
10 happy to take out any reference to that.

11 Our main point is simply to say that it would
12 be good for all parties involved to have a clear
13 standard about what it means to have facts sufficient to
14 support the probability of a misallocation. And 1807
15 does that pretty well. It's already been adopted for
16 petitions. That's really our point.

17 We're not hung up on making them contact the
18 taxpayer in every case, or even in most cases. If
19 they've got sufficient facts in their file, that's fine.

20 But we have experience that indicates that
21 we're -- you know, we're getting -- when we're reviewing
22 files as part of an appeal, we'll see the goldenrod with
23 a name and a question about whether there was a
24 misallocation being claimed as a DOK. And that's --
25 that's what we want to try to avoid is further disputes
26 between us and the staff about what constitutes a DOK
27 when they put it down in their goldenrod.

28 We think 1807's a pretty good vehicle for that,

1 but we're open to other suggestions as well.

2 MS. YEE: Okay. Thank you, Mr. Myers.

3 Other testimony, Ms. Sturdivant.

4 MS. STURDIVANT: We're in agreement with
5 MuniServices, we think that staff should be held to the
6 same standards that the cities, the local jurisdictions
7 and the consultants are held to.

8 And it's not just enough to look at an
9 allocation and think that it looks strange -- you know,
10 in writing your name and the date on a piece of paper
11 and sticking it in a file and not doing anything with it
12 for a year or 18 months. We think that staff should be
13 held to the same -- same standards and actually have
14 documentation or probability that a misallocation occurs
15 before they secure their date of knowledge.

16 MS. YEE: Okay, thank you.

17 Ms. Bouma.

18 Okay, very well. Question of staff, can you
19 comment on the consultants' approach on this?

20 MR. HUXSOLL: Well, I think we're in agreement
21 with the consultants that the information necessary to
22 operationally document a date of knowledge matches that
23 of what's necessary for a petition that a jurisdiction
24 submits and the language in the CCPM that staff --
25 staff's draft says that the operation and documented
26 date of knowledge must provide sufficient factual data
27 to support the probability that local tax has been
28 erroneously allocated and distributed. And that's

1 specifically the language for what is a valid petition
2 under 1807.

3 So, there may be question as to -- in specific
4 circumstances as to whether staff has adequately
5 documented a date of knowledge in a specific case. But
6 our position would be that the standards are the same
7 for both operationally documenting a date of knowledge
8 and a petition coming in. And we would not document a
9 date of knowledge with information that we would -- did
10 not -- for which we would not accept a petition.

11 And I think there may be concern about --

12 MS. MANDEL: Well, perhaps --

13 MR. HUXSOLL: -- specific instances.

14 MS. MANDEL: -- in the past, specific
15 instances?

16 MR. HUXSOLL: Yeah.

17 MS. MANDEL: So that maybe that's why you're
18 writing these words in the CCPM, to get away from
19 specific instances where there might have been a pending
20 fight -- may still be pending fights?

21 MS. BUEHLER: We do want to make it very clear
22 for staff what our expectations are.

23 MS. YEE: Is -- is the concern of the
24 consultants that the sufficient factual data is not
25 spelled out? Or is it -- I mean, I think we're all
26 trying to get to the same goal. And I'm a little
27 confused.

28 MS. STURDIVANT: Well, we had talked this

1 morning sometimes, you know, when we're up reviewing
2 files, whether it's -- you know, for an appeal, we'll
3 come across a goldenrod, which is what staff uses to
4 document and there'll be a name and a date and just
5 maybe a reference of, you know, a lot of money in this
6 Countywide pool. And that's used as the date of
7 knowledge.

8 That wouldn't fly for us as the date of
9 knowledge. We couldn't submit a petition just saying,
10 "Yeah, this money looks weird sitting over here." We've
11 got to identify who it belongs to, what happened in what
12 period.

13 So, sometimes what we're seeing in the file
14 doesn't seem to march the criteria that's laid out in
15 1807.

16 MS. YEE: Okay. Let me ask staff a question.
17 If -- if you were to be more explicit with respect to
18 the factual data that would be contained in the
19 explanation and pick up the language that's in -- what,
20 subdivision A of 1807 -- does that necessitate having to
21 contact the taxpayer -- any of those elements?

22 MR. HANKS: Ms. Yee, we don't believe that
23 that's necessary in all instances.

24 And it appears as though the consultants are in
25 agreement with that, that there isn't always a need to
26 contact --

27 MS. YEE: Right.

28 MR. HANKS: -- the taxpayers.

1 MS. YEE: Okay.

2 MR. HANKS: Frequently, we do.

3 But I'd like to add too, with respect to
4 Ms. Sturdivant's comment, we agree with her that, I
5 think, in years past especially there were certain
6 goldenrods that were prepared that spoke in acronyms and
7 didn't exactly lay out what staff had found in doing
8 their research in connection with exploring whether
9 reallocation was -- was necessary.

10 MS. YEE: Uh-huh.

11 MR. HANKS: We're improving training with
12 respect to that element. We're mindful that we want to
13 have the goldenrods contain the same information
14 basically that we'd expect the consultants to provide to
15 us in their petitions. So, we're on even -- even
16 footing.

17 MS. YEE: Okay. Can -- can we just kind of
18 tighten up the language maybe a little bit and have it
19 refer to "sufficient factual data consistent with the
20 requirements applicable to a petition," that is under
21 whatever that paragraph is, subdivision A of 1807? And
22 just be very, very clear that, you know, both sides same
23 factual requirements, so there's just no ambiguity? Can
24 we do that?

25 MS. BUEHLER: Uh-huh.

26 MR. HANKS: Absolutely.

27 MS. YEE: Okay, thank you.

28 Other -- discussion, Members?

1 MR. HORTON: No.

2 MS. YEE: Okay, hearing none is there a motion?

3 MR. RUNNER: I guess the motion would be move
4 as suggested.

5 MS. YEE: As amended, as proposed to be
6 amended, right?

7 MR. RUNNER: Yeah.

8 MS. YEE: All right, motion by Mr. --
9 Senator Runner to --

10 MR. HORTON: Second.

11 MS. YEE: -- move as proposed to be amended,
12 second by Mr. Horton.

13 Without objection, that motion carries. Thank
14 you.

15 Next item, Ms. Buehler.

16 MS. BUEHLER: Action item 6, the Allocation
17 Group supervisor follow-up time frames. We ask the
18 Board either staff's recommendation that the Allocation
19 Group lead follow up on assignments aged 180 to 270 days
20 and the Allocation Group supervisor follow up on
21 assignments aged greater than 270 days or MuniServices'
22 recommendation that the Allocation Group lead follow up
23 at 90 to 180 days and the Allocation Group supervisor
24 follow up after 180 days.

25 MS. YEE: Okay, thank you. Testimony on this?

26 MR. MYERS: Very brief.

27 MS. YEE: Mr. Myers, please.

28 MR. MYERS: We're -- we're okay. We -- first

1 off, I should say we very much appreciate this
2 recommendation in action 6. We think it's very much a
3 step stipulate in the right direction. It was something
4 that staff came up with and we can't give them enough
5 credit for it.

6 Our tweak was to say,

7 "Look, we have the right after 180 days
8 under 1807 to move to the next level. So,
9 wouldn't be it be better if your follow-up
10 preceded our trigger to pull it out of your
11 hands?"

12 That's all. It's not a big deal to us, we just
13 think it makes sense to follow up before the trigger
14 where we can pull it from their hands and move it to the
15 next level under 1807.

16 MS. STURDIVANT: We're in agreement with
17 MuniServices on this.

18 MS. YEE: Okay, thank you.

19 Ms. Mandel.

20 MS. MANDEL: That -- that was actually my sort
21 of question as, you know, somebody who has to manage
22 some level of workload and used to have to manage more
23 workload.

24 It did strike me as a little odd that -- that
25 there would be no follow-up. I mean I understand that
26 under the current procedures and in the past it's taken
27 some time for people to be able to work the cases.
28 Hopefully that improves over time, but --

1 MR. HANKS: Right.

2 MS. MANDEL: -- if they -- if they can pull the
3 trigger to ask Allocation Group to issue a decision on
4 six months and one day that they haven't heard anything,
5 then why would that be the time -- the same exact time
6 that a guy's going to go down the hall and say, "Hey,
7 buddy, how you coming with your workload?"

8 And maybe there's something else that goes on
9 there, but it seemed like, you know, the goal would be
10 that you're not in the position of having them pull --
11 be pulling the trigger because if they pull the trigger
12 and you only have 90 days then to finish, you know, are
13 they going to -- is that going to be the best product or
14 is stuff going to wind up going up the system into
15 Appeals that maybe could have been handled at Allocation
16 Group?

17 So, I was kind of curious for the same reason
18 as to why -- why follow-up formally in this thing wasn't
19 going to be until the trigger date. You guys said,
20 "Well, it matches the trigger date, so, it makes sense."
21 But that didn't make sense to me. So, maybe you can
22 explain it?

23 One of you.

24 MR. HANKS: Right, exactly.

25 MS. MANDEL: Kick each other under the table or
26 something.

27 MR. HANKS: Exactly. Ms. Mandel, we're --
28 we're fully supportive of having the follow up dates and

1 we're mindful that they're critical to -- to insure that
2 the work is processed in a timely manner.

3 We're also aware the trigger dates that -- that
4 are incorporated in the regulation that allows for
5 them -- for the consultants to -- to mandate that we
6 produce a decision or a -- a statement concerning
7 misallocation. But we're just also mindful of the
8 existing inventory that -- that we have.

9 We're looking to see whether or not if -- if we
10 instituted the suggested follow up dates, whether or not
11 that would add value to this review process. And it's
12 been our -- our supervisors' determination in the
13 Allocation Group Section that it would not -- just in
14 sense that some of these cases haven't necessarily had
15 the requisite amount of -- of work -- work attributable
16 to -- to some of those cases. And, so, that person's
17 review of those cases might not add that much benefit to
18 -- to the case.

19 And that -- that's why they wanted the extended
20 deadlines. Of course, this -- this could change in time
21 if -- if the thresholds were increased, I think all of
22 this somewhat goes together. If those thresholds were
23 increased to the level that staff was recommending,
24 we're thinking that our inventory levels would drop down
25 to a lower level where probably those follow-up times
26 would be more in line with what MuniServices is
27 suggesting today.

28 MS. MANDEL: Okay. And I -- you know, I don't

1 want -- I don't want through the manual to be
2 micromanaging how supervisors conduct their management
3 of their teams because everybody's different and every
4 workload's different. But I -- it was curious to me.

5 And, so, you know, there's some people that
6 work very well independently and their supervisor's not
7 going to be coming by every few days or weeks or months
8 to say, you know, "What have you done for me lately on
9 your workload?" And then probably there is some
10 managers who are going to be checking on the workload
11 before six months because that's just -- you know,
12 they're managing their unit.

13 I don't want to micromanage it, but it -- it
14 just was -- so, I'm glad to hear that, you know, they
15 don't really -- it's not a biggie to the consultants, I
16 had the same curiosity, I suppose.

17 MS. YEE: Thank you, Ms. Mandel.

18 Other discussion, Members?

19 Hearing none is there a motion?

20 MR. HORTON: So moved.

21 MS. YEE: Motion by Mr. Horton to adopt the
22 staff recommendation. Is there a second?

23 MR. RUNNER: Second.

24 MS. YEE: Second by Mr. Runner.

25 Without objection, motion carries.

26 Okay, action item 7.

27 MS. BUEHLER: Action item 7 is informing
28 jurisdictions prior to processing a large deallocation

1 of local tax resulting from a refund or credit in an
2 audit.

3 We ask the Board approve either staff's
4 recommendation that informs jurisdictions when a pending
5 refund or credit in an audit results in a deallocation
6 of \$100,000 or more in local tax to a jurisdiction or
7 HdL and MuniServices' recommendation to inform
8 jurisdictions when a pending refund or credit in an
9 audit results in a deallocation of \$50,000 or more in a
10 local tax to a jurisdiction.

11 MS. YEE: Thank you. Testimony on this item,
12 please.

13 MS. STURDIVANT: This is a suggestion that was
14 originally introduced by HdL during the interested
15 parties process. And currently a local agency doesn't
16 receive any notification at all when there's going to be
17 a large local tax deallocation as a result of a refund
18 or a credit. And we know that sometimes that these
19 deallocations can be several hundred thousand dollars,
20 which -- which really can blindsides a city. And again
21 with our current economic climate every dollar makes a
22 difference to local government agencies.

23 And we initially asked that staff use the same
24 threshold amounts for fund transfer notifications, the
25 five percent or \$50,000 of that jurisdiction's local tax
26 revenue from the prior quarter. But staff immediately
27 rejected that suggestion and instead they asked for a
28 flat amount that would apply across the board to all

1 agencies. And again because the differences in, you
2 know, how much money a large city versus a small city
3 would receive, it's really difficult to come up with a
4 number that sort of fits all across the board.

5 You know, and again some local government
6 agencies, their entire local tax revenue for a quarter
7 might be \$30,000. Because of that, we suggested 10,000.
8 Staff came become with 100,000. So, we sort of landed
9 somewhere in the middle at 50.

10 But we still question how a notification amount
11 this large will assist a smaller jurisdiction with their
12 budget and planning. \$50,000, that's a staff salary.

13 And again this is another case where -- where
14 staff is concerned with workload but the local
15 government agency is concerned with how to best manage
16 the funds that they have to provide the services that
17 they need for the citizens in their community.

18 MS. YEE: Okay, thank you, Ms. Sturdivant.

19 Other testimony? Mr. Myers.

20 MR. MYERS: Yes, we would just like to -- we
21 support HdL and also appreciate staff being willing to
22 work us with in this new area.

23 So, we support HdL's position on this.

24 MS. YEE: Thank you. Senator Runner.

25 MR. RUNNER: Yeah, I mean I think it's a good
26 tool and is welcome by -- by the local governments at
27 that point.

28 And, so, now the the discussion is -- is with

1 something that's new, is the line better at 50 or 100?
2 Let me just, again, say I've got lots of little
3 communities out there in my district. And if you're
4 going to open up this as a -- because it has a -- if
5 this is a policy we're moving forward on because we
6 believe the local governments deserve and this will help
7 them operate better, then it seems to me we need to then
8 decide what that number is that makes sense.

9 And I think the \$100,000 is too high. I -- we
10 asked for some additional background on this and found
11 that if you go from 100 down to 50 that there's twelve
12 additional contacts that would have had to have been
13 made in the last calendar year, I think. That's one a
14 month. I can't imagine that that is a big workload
15 problem. So, I'm compelled to feel like \$50,000 is a
16 reasonable good policy if we believe that this is an
17 important policy to move forward with.

18 MS. YEE: Thank you, Senator Runner. Other
19 discussion?

20 MS. MANDEL: Sure.

21 MS. YEE: Ms. Mandel, please.

22 MS. MANDEL: Thanks for getting the information
23 in advance.

24 Yeah, I -- I was interested in the 50 to
25 100,000 split in terms of workload, and, so, thank you
26 for the information.

27 And we do -- you know, there was a -- a couple
28 of years ago when the Board delegation went to 100 -- to

1 the \$100,000. We still have any refund or credit --
2 there's supposed to be a public record of that kept, I
3 forget where that is, whether that's in the Executive
4 Office or Board Proceedings, I forget at the instant
5 moment.

6 But -- but -- so, those ones where that number
7 is happening, are being called out and -- at least if
8 you're doing what you're supposed to be doing and the
9 public record being kept somewhere. So, it's not like
10 you're going to go looking for what ones are at -- what
11 ones are at that level and that is just however many of
12 those there are, whether there's reallocation impact
13 which, by virtue of having to -- I would think by virtue
14 of having to pull that one to make the public record,
15 you would know, "Oh, yeah, this is one where we had some
16 level of reallocation."

17 'Cause it's a warning system, right, just so
18 they know it's going --

19 MS. BUEHLER: A courtesy.

20 MS. MANDEL: -- come?

21 MS. YEE: Yeah.

22 MS. MANDEL: Yeah.

23 MR. HANKS: Right. Ms. Mandel, we're -- we're
24 certainly sensitive to the locals needing this
25 information and we're -- we're receptive to that.

26 We're -- we're in a position where we do
27 recommend the \$100,000 threshold, however. We want to
28 supply that information to them because we recognize

1 that -- that that type of a deallocation can be
2 significant to any size city. It -- currently this
3 notification is not given to cities.

4 MS. MANDEL: No, we -- we understand that.

5 But I'm trying to justify the going from -- not
6 not doing 50 when every credit or refund that is, I
7 guess, over 50,000 -- so, it's not right at 50,000, it's
8 over 50,000 -- gets a public record made of it and kept
9 somewhere. Because the justification for 100 was those
10 are the ones that have to come to the Board now for
11 approval and, so, we're already doing something manual
12 by writing the little -- you know, whatever information
13 you give us for the Board meeting.

14 And my question was, but you have to pull out
15 the ones that are over 50, even if they're not the 100s,
16 but the over 50 to 100 to make the public record.

17 So, I was just curious why the same -- we're
18 already pulling it out, isn't -- to make the public
19 record, doesn't have the same -- we're already looking
20 at it for some manual purpose.

21 MR. HANKS: Ms. Mandel, in -- in terms of the
22 public record that -- that's maintained in Board
23 Proceedings, the information that's captured in those
24 public notifications isn't -- isn't detailed enough for
25 you to note that -- that there's going to be a
26 deallocation within a particular --

27 MS. MANDEL: Not detailed enough for someone
28 who looks at the public record 'cause that's not the

1 purpose of that public record.

2 MR. HANKS: Correct.

3 MS. MANDEL: But maybe I don't know how you're
4 doing them.

5 Is it just something that's a computer run and
6 gets sent -- gets sent there or is something where
7 there's -- you know, the justification on 100,000 again
8 was that there's something manual that staff has to go,

9 "Oh, this one's 100,000, I have to pull it.

10 I have to, you know, do something for Board
11 meeting, therefore, it's not big deal for me to
12 also just send out a courtesy letter, if that
13 one involves a change in the allocation."

14 And 50,000 -- over 50,000 going to public
15 record, if those are -- if that's just a computer run
16 that's going, then nobody's pulling those to then put
17 them onto some type of typed up little thing that
18 goes -- you see what I'm saying?

19 I'm just -- I felt like we were -- you were
20 touching them already to send them to wherever they're
21 going for the public record and touching them already,
22 what -- what's so hard about a courtesy level -- letter
23 then if -- if a particular one involves a deallocation?

24 MR. HANKS: I see. Ms. Mandel, the cases that
25 get scheduled for Board consideration are in excess of
26 \$100,000. So, that's -- that's going to be any -- any
27 refund, sales and -- and local tax and transactions tax.

28 So, we're -- in the proposal that we're

1 discussing this morning, we're talking about just
2 exclusively the \$100,000 in local tax that -- that's
3 going to be deallocated or the \$50,000 that's going to
4 be deallocated from a certain jurisdiction.

5 Now, we've got large taxpayers that -- that
6 would probably be the ones that -- that are triggering
7 either of those two thresholds. And what we typically
8 have is these large taxpayers reporting sales via the
9 sales locations of various locations throughout
10 California. And what they're going to be doing is
11 allocating the local tax to the Countywide pools.

12 Now, what we would have in the information that
13 we've got is -- is just the run number that was
14 allocated to that -- that County pool. Let's say it's
15 Los Angeles County. We've got numerous cities within
16 Los Angeles County. So, what staff would have to do is
17 to look at the proportionate share of local tax that's
18 being given to the City of Los Angeles, the City of
19 Azusa, I mean, every city within Los Angeles County to
20 determine where -- where that -- where those amounts
21 lie. And then we would have to compare the refund sum
22 against those -- those amounts to see if we have
23 exceeded a \$50,000 threshold or \$100,000 threshold. And
24 all of these calculations would have to be done
25 manually.

26 In the future, certainly, this could be
27 something that -- that we could probably incorporate
28 into CROS, but currently it is a manual process.

1 MS. MANDEL: Okay. Maybe -- I guess then I was
2 confused by focusing on the 50,000 refund because the
3 50,000 refund is all tax together, not just --

4 MR. HANKS: All tax.

5 MS. MANDEL: -- not just the 1 percent --

6 MR. HANKS: Correct, correct.

7 MS. MANDEL: -- local. So, you are talking
8 about a -- and I'm sorry then I got confused because you
9 referenced in the paper the 100,000 threshold that's for
10 the Board and that is total --

11 MR. HANKS: Total tax.

12 MS. MANDEL: -- total tax. So -- so, every
13 single one of -- okay.

14 So, it -- so, so -- so, it would necessarily,
15 even at a \$50,000 limit, it would necessarily then be
16 ones where the -- where it's going to, under our current
17 delegation, it would -- it would necessarily be one
18 that's on a Board agenda?

19 MR. HANKS: Correct.

20 MS. MANDEL: Because it's only the local tax
21 portion?

22 MR. HANKS: Correct.

23 MS. MANDEL: So, now you're talking about we're
24 going to pull all the ones that are on the Board agenda,
25 but then only send a courtesy letter if -- to any
26 particular jurisdiction that's 100,000?

27 MR. HANKS: Correct.

28 MS. MANDEL: And in the situation where you

1 have a Countywide Pool, is the issue is -- your example,
2 it would seem to me that rather than doing --
3 necessarily doing every single one if it's going from
4 Countywide to a place, I would think you'd start with
5 whoever gets the biggest nut out of the Countywide Pool.
6 And if it doesn't -- if they don't hit the threshold,
7 you're not going to do all the other guys. You're just
8 going to go, "Oh, well, it's -- "

9 Again I'm having trouble understanding what the
10 workload impact really is, I mean, how big it really is
11 to do it.

12 MR. RUNNER: Again, for the sake of a long
13 agenda, I would like to --

14 MS. MANDEL: Sorry I'm talking so much.

15 MR. RUNNER: -- no, no, it's all of us, it's
16 okay.

17 I'd like to make a motion that we --

18 MR. HORTON: Second.

19 MR. RUNNER: -- that we -- that we create the
20 threshold at \$50,000.

21 MS. YEE: All right. Motion by Mr. Runner to
22 establish the threshold -- essentially the HdL's and
23 MuniServices' recommendation then at \$50,000.

24 Is there a second?

25 MR. HORTON: Second.

26 MS. YEE: Second by Mr. Horton.

27 Without objection, motion carries.

28 MS. YEE: Okay. Ms. Buehler, I think that

1 dispenses with this item, yes?

2 MS. BUEHLER: Yes, it does.

3 MS. YEE: Or this agenda item, okay.

4 Our next issue? Thank you.

5 MS. BUEHLER: Agenda item 3, Randy Ferris from
6 our Legal Department will be joining me.

7 MS. YEE: Okay, we have two speakers on this
8 item, if Miss Rodriguez and Mr. Rivera would come
9 forward?

10 Okay, good afternoon, Mr. Ferris.

11 MR. FERRIS: I think Susanne has some
12 introductory comments.

13 MS. BUEHLER: I do.

14 MS. YEE: Please.

15 MS. BUEHLER: We would like to provide an
16 update on the software technology transfer agreement
17 study with industry that the Board approved at the
18 August 2011 meeting.

19 In cooperation with industry, the study was to
20 determine the feasibility of adopting an optional
21 percentage that can be applied to the technology
22 transfer agreements lump sum sales price to estimate the
23 amount paid for the tangible personal property
24 transferred under the technology transfer agreement.

25 In regard to the the study, staff sent an
26 invitation to approximately 300 prospective participants
27 and interested parties asking them to participate in the
28 study. We posted information about tech -- software

1 technology transfer agreements on the Board of
2 Equalization website.

3 To date, one company has volunteered to
4 participate in the study. Although the participant
5 could provide valuable information, we do not believe it
6 would be appropriate to establish an industry standard
7 based only on one company's data.

8 Staff has contacted a number of companies to
9 determine if there were specific reasons they were not
10 willing to participate in the study. Based on these
11 discussions it appears many potential participants are
12 reluctant to have Board staff review their records
13 without specifics on what will be reviewed.

14 Because of the lack of interest by industry in
15 completing the study, we are requesting your approval to
16 begin an interested parties process to discuss whether
17 it is necessary to amend Regulation 1507 to explain when
18 an agreement involving the transfer of software on
19 tangible storage media qualifies as a technology
20 transfer agreement and how tax applies to the sale of
21 tangible personal property transferred in a software
22 technology transfer agreement.

23 MS. YEE: Thank you very much. Let's hear from
24 our speakers and then we'll open it up for discussion.

25 Good afternoon.

26 ---o0o---

27

28

1 GUS RIVERA

2 INTEL CORPORATION

3 ---o0o---

4 MR. RIVERA: Good afternoon, Madam Chair and
5 Members.

6 My name's Gus Rivera. I'm with Intel
7 Corporation and also representing the Silicon Valley
8 Leadership Group.

9 I'm actually here to strongly support the
10 staff's request for the interested parties process for
11 this particular issue. And that's about it.

12 MS. YEE: Okay, thank you very much.
13 Miss Rodriquez.

14 ---o0o---

15 GINA RODRIQUEZ

16 CALIFORNIA TAXPAYERS' ASSOCIATION

17 ---o0o---

18 MS. RODRIQUEZ: Thank you. Gina Rodriquez with
19 California Taxpayers' Association.

20 Ditto what Gus said. We are in strong support
21 of moving forward with the interested parties process.

22 I do want to note that Susanne stated that
23 there's a lack of interest in completing this study and
24 there really isn't a lack of interest. We are fully
25 committed to completing the study. We just need to have
26 the right questions posed. And, so, maybe through an
27 interested parties process we can have that -- have that
28 happen.

1 Thank you.

2 MS. YEE: Thank you.

3 Discussion, Members? Ms. Mandel.

4 MS. MANDEL: Sure. I -- I mean I appreciate
5 staff's sending out letters and making follow-up calls,
6 but it's -- you know, it's a complicated area. The
7 letters can sometimes be dense. They can get lost on
8 people's desks and they may not realize they even
9 received one or that it was what they were supposed to
10 be looking for.

11 So, I think talking -- you can tell I like to
12 talk sometimes -- but it's -- it's often underrated in
13 this era of, you know, e-mails, et cetera. It -- it is
14 a -- it is our earliest and sometimes our best
15 communication device.

16 So, I look forward to the interested parties
17 process.

18 MS. YEE: Okay. Thank you, Ms. Mandel.

19 Other -- Senator Runner.

20 MR. RUNNER: Move to move forward with the
21 interested parties process.

22 MS. YEE: Okay. A motion by Mr. Runner to move
23 forward with the interested parties process, is there a
24 second?

25 MR. HORTON: Second, but Madam Chair --

26 MS. YEE: Yes, please, Mr. Horton.

27 MR. HORTON: -- you know, I just wanted to
28 first say to the Department that they -- they actually

1 did a -- they did a good job in reaching out to the
2 industry. There was conversation that occurred and
3 communications to the industry relative to the desire to
4 address this issue. And, so, it's good that we are
5 coming forward.

6 And it was was that conversation and the
7 ultimate communications that actually ignited or was the
8 the catalyst for the discussions that are occurring now.

9 And certainly I want to encourage the -- well,
10 not encourage because they are at a point that they've
11 -- as I've suggested in the past, and many of us as
12 well, is that they're at a point where they've
13 consolidated their -- their efforts into one organized
14 body that can speak on behalf of that entity. And I
15 think that a -- that that would be very helpful.

16 But it is the process that we've gone through
17 thus far that's gotten us to this point. And, so, both
18 parties -- I want to thank both parties for their
19 participation to the extent that that did exist.

20 MS. YEE: Yeah.

21 MR. HORTON: Thank you very much.

22 MS. YEE: Thank you. I'll add my
23 acknowledgement of the staff as well.

24 I'd like to make an additional request. I know
25 we have a motion and a second on the table, but with
26 respect to, I guess, the sensitivity of this issue, I'd
27 like to actually see an update to the Board or maybe a
28 status report after the first interested parties

1 meeting, just so we get a sense of where we're headed,
2 sensitive to, obviously, because there are other moving
3 parts that are not going to be subject, I hope, of that
4 interested parties discussion.

5 MR. FERRIS: That's correct.

6 MS. YEE: Okay, thank you.

7 MS. BUEHLER: Yes.

8 MS. YEE: Okay. We have motion and a second,
9 without objection?

10 Motion carries. Thank you much,

11 I think, Ms. Olson, that concludes the Business
12 Taxes Committee.

13 MS. OLSON: Thank you.

14 MS. YEE: Thank you, Members.

15 ---000---

**ESTIMATE OF COST OR SAVINGS RESULTING
FROM PROPOSED REGULATORY ACTION**

Proposed Amendment of Sales and Use Tax Regulation 1618, *United States Government Supply Contracts*

STATEMENT OF COST OR SAVINGS FOR NOTICE OF PUBLIC HEARING

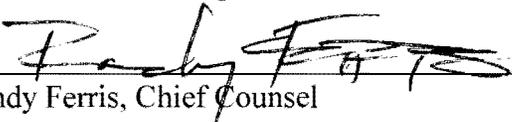
The State Board of Equalization has determined that the proposed action does not impose a mandate on local agencies or school districts. Further, the Board has determined that the action will result in no direct or indirect cost or savings to any State agency, any local agency or school district that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

The cost impact on private persons or businesses will be insignificant. This proposal will not have a significant adverse economic impact on businesses.

This proposal will not be detrimental to California businesses in competing with businesses in other states.

This proposal will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses or create or expand business in the State of California.

Statement
Prepared by  Date 4/6/12
Richard Bennion, Regulations Coordinator

Approved by  Date 4/6/12
Randy Ferris, Chief Counsel

If Costs or Savings are Identified, Signatures of Chief, Fiscal Management Division, and Chief, Board Proceedings Division, are Required

Approved by _____ Date _____
Chief, Financial Management Division

Approved by _____ Date _____
Chief, Board Proceedings Division

NOTE: SAM Section 6660 requires that estimates resulting in cost or savings be submitted for Department of Finance concurrence before the notice of proposed regulatory action is released.

ECONOMIC AND FISCAL IMPACT STATEMENT

(REGULATIONS AND ORDERS)

STD. 399 (REV. 12/2008)

See SAM Section 6601 - 6616 for Instructions and Code Citations

AGENCY NAME Board of Equalization	CONTACT PERSON Richard E. Bennion	TELEPHONE NUMBER 916-445-2130
DESCRIPTIVE TITLE FROM NOTICE REGISTER OR FORM 400 Title 18, Section 1618, United States Government Supply Contracts		NOTICE FILE NUMBER Z

ECONOMIC IMPACT STATEMENT

A. ESTIMATED PRIVATE SECTOR COST IMPACTS (Include calculations and assumptions in the rulemaking record.)

1. Check the appropriate box(es) below to indicate whether this regulation:

- a. Impacts businesses and/or employees
- b. Impacts small businesses
- c. Impacts jobs or occupations
- d. Impacts California competitiveness
- e. Imposes reporting requirements
- f. Imposes prescriptive instead of performance
- g. Impacts individuals
- h. None of the above (Explain below. Complete the Fiscal Impact Statement as appropriate.)

h. (cont.) Please see the attached .

(If any box in Items 1 a through g is checked, complete this Economic Impact Statement.)

2. Enter the total number of businesses impacted: _____ Describe the types of businesses (Include nonprofits.): _____

Enter the number or percentage of total businesses impacted that are small businesses: _____

the number of businesses that will be created: _____ eliminated: _____

Explain: _____

4. Indicate the geographic extent of impacts: Statewide Local or regional (List areas.): _____

5. Enter the number of jobs created: _____ or eliminated: _____ Describe the types of jobs or occupations impacted: _____

6. Will the regulation affect the ability of California businesses to compete with other states by making it more costly to produce goods or services here?

Yes No If yes, explain briefly: _____

B. ESTIMATED COSTS (Include calculations and assumptions in the rulemaking record.)

1. What are the total statewide dollar costs that businesses and individuals may incur to comply with this regulation over its lifetime? \$ _____

a. Initial costs for a small business: \$ _____ Annual ongoing costs: \$ _____ Years: _____

b. Initial costs for a typical business: \$ _____ Annual ongoing costs: \$ _____ Years: _____

c. Initial costs for an individual: \$ _____ Annual ongoing costs: \$ _____ Years: _____

Describe other economic costs that may occur: _____

ECONOMIC AND FISCAL IMPACT STATEMENT cont. (STD. 399, Rev. 12/2008)

2. If multiple industries are impacted, enter the share of total costs for each industry: _____

3. If the regulation imposes reporting requirements, enter the annual costs a typical business may incur to comply with these requirements. (Include the dollar costs to do programming, record keeping, reporting, and other paperwork, whether or not the paperwork must be submitted.): \$ _____

4. Will this regulation directly impact housing costs? Yes No If yes, enter the annual dollar cost per housing unit: _____ and the number of units: _____

5. Are there comparable Federal regulations? Yes No Explain the need for State regulation given the existence or absence of Federal regulations: _____

Enter any additional costs to businesses and/or individuals that may be due to State - Federal differences: \$ _____

C. ESTIMATED BENEFITS (Estimation of the dollar value of benefits is not specifically required by rulemaking law, but encouraged.)

1. Briefly summarize the benefits that may result from this regulation and who will benefit: _____

2. Are the benefits the result of: specific statutory requirements, or goals developed by the agency based on broad statutory authority?
Explain: _____

3. What are the total statewide benefits from this regulation over its lifetime? \$ _____

D. ALTERNATIVES TO THE REGULATION (Include calculations and assumptions in the rulemaking record. Estimation of the dollar value of benefits is not specifically required by rulemaking law, but encouraged.)

1. List alternatives considered and describe them below. If no alternatives were considered, explain why not: _____

2. Summarize the total statewide costs and benefits from this regulation and each alternative considered:

Regulation:	Benefit: \$ _____	Cost: \$ _____
Alternative 1:	Benefit: \$ _____	Cost: \$ _____
Alternative 2:	Benefit: \$ _____	Cost: \$ _____

3. Briefly discuss any quantification issues that are relevant to a comparison of estimated costs and benefits for this regulation or alternatives: _____

4. Rulemaking law requires agencies to consider performance standards as an alternative, if a regulation mandates the use of specific technologies or equipment, or prescribes specific actions or procedures. Were performance standards considered to lower compliance costs? Yes No
Explain: _____

E. MAJOR REGULATIONS (Include calculations and assumptions in the rulemaking record.) Cal/EPA boards, offices, and departments are subject to the following additional requirements per Health and Safety Code section 57005.

ECONOMIC AND FISCAL IMPACT STATEMENT cont. (STD. 399, Rev. 12/2008)

1. Will the estimated costs of this regulation to California business enterprises exceed \$10 million? Yes No (If No, skip the rest of this section.)

efly describe each equally as an effective alternative, or combination of alternatives, for which a cost-effectiveness analysis was performed:

Alternative 1: _____

Alternative 2: _____

3. For the regulation, and each alternative just described, enter the estimated total cost and overall cost-effectiveness ratio:

Regulation: \$ _____ Cost-effectiveness ratio: \$ _____
Alternative 1: \$ _____ Cost-effectiveness ratio: \$ _____
Alternative 2: \$ _____ Cost-effectiveness ratio: \$ _____

FISCAL IMPACT STATEMENT

A. FISCAL EFFECT ON LOCAL GOVERNMENT (Indicate appropriate boxes 1 through 6 and attach calculations and assumptions of fiscal impact for the current year and two subsequent Fiscal Years.)

1. Additional expenditures of approximately \$ _____ in the current State Fiscal Year which are reimbursable by the State pursuant to Section 6 of Article XIII B of the California Constitution and Sections 17500 et seq. of the Government Code. Funding for this reimbursement:

a. is provided in _____, Budget Act of _____ or Chapter _____, Statutes of _____

b. will be requested in the _____ Governor's Budget for appropriation in Budget Act of _____ (FISCAL YEAR)

Additional expenditures of approximately \$ _____ in the current State Fiscal Year which are not reimbursable by the State pursuant to Section 6 of Article XIII B of the California Constitution and Sections 17500 et seq. of the Government Code because this regulation:

a. implements the Federal mandate contained in _____

b. implements the court mandate set forth by the _____ court in the case of _____ vs. _____

c. implements a mandate of the people of this State expressed in their approval of Proposition No. _____ at the _____ election; (DATE)

d. is issued only in response to a specific request from the _____, which is/are the only local entity(s) affected;

e. will be fully financed from the _____ (FEES, REVENUE, ETC.) authorized by Section _____ of the _____ Code;

f. provides for savings to each affected unit of local government which will, at a minimum, offset any additional costs to each such unit;

g. creates, eliminates, or changes the penalty for a new crime or infraction contained in _____

Savings of approximately \$ _____ annually.

4. No additional costs or savings because this regulation makes only technical, non-substantive or clarifying changes to current law regulations.

ECONOMIC AND FISCAL IMPACT STATEMENT cont. (STD. 399, Rev. 2-98)

5. No fiscal impact exists because this regulation does not affect any local entity or program.
6. Other.

B. FISCAL EFFECT ON STATE GOVERNMENT (Indicate appropriate boxes 1 through 4 and attach calculations and assumptions of fiscal impact for the current year and two subsequent Fiscal Years.)

1. Additional expenditures of approximately \$ _____ in the current State Fiscal Year. It is anticipated that State agencies will:
- a. be able to absorb these additional costs within their existing budgets and resources.
- b. request an increase in the currently authorized budget level for the _____ fiscal year.
2. Savings of approximately \$ _____ in the current State Fiscal Year.
3. No fiscal impact exists because this regulation does not affect any State agency or program.
4. Other.

C. FISCAL EFFECT ON FEDERAL FUNDING OF STATE PROGRAMS (Indicate appropriate boxes 1 through 4 and attach calculations and assumptions of fiscal impact for the current year and two subsequent Fiscal Years.)

1. Additional expenditures of approximately \$ _____ in the current State Fiscal Year.
2. Savings of approximately \$ _____ in the current State Fiscal Year.
3. No fiscal impact exists because this regulation does not affect any federally funded State agency or program.
4. Other.

SIGNATURE 	TITLE Regulations Coordinator
AGENCY SECRETARY ¹ APPROVAL/CONCURRENCE	DATE 4/5/12
DEPARTMENT OF FINANCE ² APPROVAL/CONCURRENCE Exempt under SAM section 6660	DATE

1. The signature attests that the agency has completed the STD. 399 according to the instructions in SAM sections 6600-6680, and understands the impacts of the proposed rulemaking. State boards, offices, or departments not under an Agency Secretary must have the form signed by the highest ranking official in the organization.
2. Finance approval and signature is required when SAM sections 6600-6670 require completion of the Fiscal Impact Statement in the STD. 399.

Attachment to Economic and Fiscal Impact
Statement (STD. 399 (Rev. 12/2008)) for the Proposed Amendments to
California Code of Regulations, Title 18, Section 1618,
United States Government Supply Contracts

Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, Revenue and Taxation Code (RTC) section 6007 provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business" and RTC section 6381 provides a sales tax exemption for gross receipts from the sale of tangible personal property to the United States.

California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*, prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor's business (hereafter, "sales for resale to the United States"). The regulation generally provides that:

- A retailer's sales of tools, equipment, direct consumable supplies and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer's sales of tools, equipment, direct consumable supplies and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

Regulation 1618 also provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in chapter 1 of title 48 of the Code of Federal Regulations, the Federal Acquisition Regulation (FAR); and Regulation 1618 provides specific guidance as to when title to "special tooling" passes to the United States under the FAR.

Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal's decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to "special tooling" passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for "special tooling," and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007.

The State Board of Equalization's (Board's) proposed amendments make Regulation 1618 consistent with the 2007 amendments to the FAR by:

- Deleting the provisions in subdivision (a)(2) providing that the term "tools," as used in the definition of "direct consumable supplies," does not include "special tooling";
- Adding new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term "tools," as used in the definition of "direct consumable supplies," includes "special tooling" that was previously covered by FAR part 52.245-17; and
- Amending the second to last sentence in subdivision (b) to reflect that the FAR's title passage clauses for "special tooling" applied until Jun 13, 2007, but were no longer effective after that date.

The Board's proposed amendments to Regulation 1618 clarify that costs for "overhead materials" must be allocated to United States Government supply contracts "consistent with government cost accounting standards." The Board's proposed amendments also clarify the guidance provided in subdivision (b) of the regulation regarding the passage of title to "direct consumable supplies" and "overhead materials" by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of indirect consumable supplies, and providing distinct guidance regarding the passage of title to direct consumable supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

Furthermore, the proposed amendments are consistent with RTC sections 6007 and 6381, the proposed amendments are consistent with the FAR, and the Aerospace Industries Association (AIA) collaborated with Board staff in the development of the proposed amendments and AIA agreed with the proposed amendments. Therefore, based upon the foregoing information and all of the information in the rulemaking file, the Board has determined that the adoption of the proposed amendments to Regulation 1618:

- Will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states;
- Will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California;
- Will not have a significant effect on housing costs;
- Will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California; and
- Will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

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

NOTICE PUBLICATION/REGULATIONS SUBMISSION

(See instructions on reverse)

For use by Secretary of State only

STD. 400 (REV. 01-09)

OAL FILE NUMBERS	NOTICE FILE NUMBER Z-2012-0406-01	REGULATORY ACTION NUMBER	EMERGENCY NUMBER
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For use by Office of Administrative Law (OAL) only

RECEIVED FOR FILING PUBLICATION DATE

APR 06 '12 APR 20 '12

Office of Administrative Law

NOTICE

REGULATIONS

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 United States Government Supply Contracts		TITLE(S) 18	FIRST SECTION AFFECTED 1618	2. REQUESTED PUBLICATION DATE April 20, 2012	
3. NOTICE TYPE <input checked="" type="checkbox"/> Notice re Proposed Regulatory Action <input type="checkbox"/> Other		4. AGENCY CONTACT PERSON Richard E. Bennion		TELEPHONE NUMBER (916) 445-2130	FAX NUMBER (Optional) (916) 324-3984
OAL USE ONLY	ACTION ON PROPOSED NOTICE <input type="checkbox"/> Approved as Submitted <input type="checkbox"/> Approved as Modified <input type="checkbox"/> Disapproved/Withdrawn			NOTICE REGISTER NUMBER	PUBLICATION DATE

B. SUBMISSION OF REGULATIONS (Complete when submitting regulations)

1a. SUBJECT OF REGULATION(S)	1b. ALL PREVIOUS RELATED OAL REGULATORY ACTION NUMBER(S)
------------------------------	--

IF CALIFORNIA CODE OF REGULATIONS TITLE(S) AND SECTION(S) (Including title 26, if toxics related)

ACTION(S) AFFECTED (List all section number(s) individually. Attach additional sheet if needed.)	ADOPT
	AMEND
	REPEAL
TITLE(S)	

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 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 30th day after filing with Secretary of State	<input type="checkbox"/> Effective on filing with Secretary of State	<input 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	TELEPHONE NUMBER	FAX NUMBER (Optional)	E-MAIL ADDRESS (Optional)
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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.

For use by Office of Administrative Law (OAL) only

SIGNATURE OF AGENCY HEAD OR DESIGNEE	DATE
TYPED NAME AND TITLE OF SIGNATORY	

Notice of Proposed Regulatory Action

The State Board of Equalization Proposes to Adopt Amendments to California Code of Regulations, Title 18, Section 1618, *United States Government Supply Contracts*

NOTICE IS HEREBY GIVEN

The State Board of Equalization (Board), pursuant to the authority vested in it by Revenue and Taxation Code (RTC) section 7051, proposes to adopt amendments to California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*. Regulation 1618 implements, interprets, and makes specific RTC section 6207, which provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business," and RTC section 6381, which provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States. The proposed amendments make the regulation consistent with the 2007 amendments to the Federal Acquisition Regulation (FAR) codified in chapter 1 of title 48 of the Code of Federal Regulations, and clarify the requirements for making sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 26-28, 2012. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at www.boe.ca.gov at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 9:30 a.m. or as soon thereafter as the matter may be heard on June 26, 27, or 28, 2012. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1618.

AUTHORITY

RTC section 7051.

REFERENCE

RTC sections 6007 and 6381.

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

Current Regulation 1618

Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, RTC section 6007 provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business" and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

Regulation 1618 currently prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor's business (hereafter, "sales for resale to the United States"). The regulation generally provides that:

- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

Regulation 1618 also currently provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in the FAR, and Regulation 1618 provides specific guidance as to when title to "special tooling" passes to the United States under the FAR.

2007 Amendments to FAR

Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal's decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to "special tooling" passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for "special tooling," and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007.

Effect, Objectives, and Benefits of the Proposed Amendments to Regulation 1618

The Board directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts. At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR, and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term “tools,” as used in the definition of direct consumable supplies, does not include “special tooling”;
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term “tools,” as used in the definition of direct consumable supplies, includes “special tooling” that “was previously covered by FAR part 52.245-17”; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR’s title passage clauses for special tooling applied until Jun 13, 2007, but were no longer effective after that date.

In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for “overhead materials” must be allocated to United States Government supply contracts “consistent with government cost accounting standards.” It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to “direct consumable supplies” and “overhead materials” by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of “indirect consumable supplies,” and providing distinct guidance regarding the passage of title to direct consumable supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

The Aerospace Industries Association (AIA) participated in Board staff’s meetings with the interested parties and AIA agreed with staff’s recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

During its March 20, 2012, Business Taxes Committee meeting, the Board determined that staff’s recommended amendments are reasonably necessary to accomplish the objectives of making Regulation 1618 consistent with the 2007 amendments to the FAR and clarifying Regulation 1618’s guidance regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials. The proposed amendments are anticipated to provide the following specific benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;

2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1618 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1618 is the only state regulation prescribing the requirements for making sales for resale to the United States. In addition, there is no federal sales tax and there are no comparable federal regulations or statutes to Regulation 1618.

NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

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

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The proposed amendments to Regulation 1618 make the regulation consistent with the 2007 amendments to the FAR, eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR, and provide more clarity and certainty regarding the requirements for sales for resale of direct consumable supplies and indirect consumable supplies, including overhead materials, to the United States. The proposed amendments were the result of a collaborative effort between Board staff and the interested parties and are intended to provide additional certainty to retailers. Furthermore, the proposed amendments will not impose any new taxes. Therefore, the Board has made an initial determination that the adoption of the proposed amendments to Regulation 1618 will not have a significant, statewide adverse economic impact directly

affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulation 1618 may affect small business.

NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

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

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

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1618 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulation 1618 will not affect the health and welfare of California residents, worker safety, or the state's environment.

NO SIGNIFICANT EFFECT ON HOUSING COSTS

Adoption of the proposed amendments to Regulation 1618 will not have a significant effect on housing costs.

DETERMINATION REGARDING ALTERNATIVES

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

CONTACT PERSONS

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at Bradley.Heller@boe.ca.gov, or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at

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

WRITTEN COMMENT PERIOD

The written comment period ends at 9:30 a.m. on June 26, 2012, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulation 1684 during the June 26-28, 2012, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1618. The Board will only consider written comments received by that time.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared an underscored and strikeout version of the text of Regulation 1618 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at www.boe.ca.gov.

SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The Board may adopt the proposed amendments to Regulation 1618 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed amendments, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulation 1618, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at www.boe.ca.gov.

**Text of Proposed Amendments to
California Code of Regulations, Title 18, Section 1618**

Section 1618. United States Government Supply Contracts.

(a) Definitions.

(1) "United States Government supply contract" means a contract with the United States to furnish, or to fabricate and furnish, tangible personal property including ships, aircraft, ordnance, or equipment, whereby title to tangible personal property purchased for use in fulfilling the contract passes to the United States pursuant to the title provisions contained in the contract before the contractor uses the property to perform the function or act for which the property was designed or manufactured. The term "U.S. Government supply contract" does not include contracts to construct improvements on or to real property or to the purchase of tangible personal property for use in fulfilling such contracts.

(2) "Direct consumable supplies" means supplies, tools, or equipment consumed in the performance of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~"Tools" as used in this definition does not include "special tooling" subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17.~~ Effective June 14, 2007, "Tools" as used in this definition includes "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.

(3) "Overhead materials" means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

(2) Whether title to direct consumable supplies ~~and~~ or indirect consumable supplies (i.e., overhead materials) passes to the United States under a United States government supply contract and the time at which title passes will be determined in

accordance with the title provisions contained in the contract, if any. ~~In a case where the cost of~~

(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

(B) For indirect consumable supplies (i.e., overhead materials), which are charged to an expense account which is then allocated to various locations, cost centers or contracts, ~~some of which are engaged in other than United States government cost reimbursement contracts and/or fixed price contracts with a progress payments clause,~~ it will be considered that title ~~did not pass~~ to the United States government prior to use of the property, and tax will not apply with respect to the purchase or use of the property charged to the expense account, ~~unless~~ if the item is ~~specifically accounted for as being charged~~ allocated to a specific United States government supply contract, pursuant to the terms of which title passes to the United States prior to the use of the item. Property will be considered ~~charged~~ allocated to a specific United States government supply contract when it is allocated pursuant to:

(1) a1. Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,

(2) g2. Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in ~~this~~ the manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

(3) Special Tooling. Effective December 29, 1989 through June 13, 2007, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17. Title to such special tooling will pass prior to use by the contractor only if the agreement between the contractor and the United States government contains a custom clause providing for title passage prior to use by the contractor. Therefore, sales of special tooling will generally be subject to tax.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6007 and 6381, Revenue and Taxation Code; and Aerospace Corp. v. St. Bd. of Equalization (1990) 218 Cal.App.3d 1300.

Bennion, Richard

From: BOE-Board Meeting Material
Sent: Friday, April 20, 2012 8:48 AM
To: Alonzo, Mary Ann (Legal); Anderson, Karen E.; Angeles, Joel; Bartolo, Lynn; Bennion, Richard; Bisauta, Christine (Legal); Blake, Sue; BOE-Board Meeting Material; Boring, Dilara; Carey, Lynne; Chung, Sophia (Legal); Davis, Toya P.; Delgado, Maria; Duran, David; Elliott, Claudia; Epolite, Anthony (Legal); Evans, Regina; Ferris, Randy (Legal); Garcia, Laura; Gau, David; Gilman, Todd; Giorgi, Dolores; Goehring, Teresa; Hale, Mike; Hall, Gail; Hanohano, Rebecca; Harvill, Mai; He, Mengjun; Heller, Bradley (Legal); Hellmuth, Leila; Herrera, Cristina; Holmes, Dana; Hughes, Shellie L; Ingenito, Robert; Jacobson, Andrew; Kinkle, Sherrie L; Kuhl, James; Lambert, Robert (Legal); Levine, David H. (Legal); LoFaso, Alan; Maddox, Ken; Madrigal, Claudia; Maeng, Elizabeth; Mandel, Marcy Jo; Matsumoto, Sid; Mayhew, Heather; McGuire, Jeff; Miller, Brad; Mandel, Marcy Jo @ SCO; Moon, Richard (Legal); Morquecho, Raymond; Nienow, Trecia (Legal); Ralston, NaTasha; Richmond, Joann; Riley, Denise (Legal); Schultz, Glenna; Scott, Megan; Shah, Neil; Singh, Sam; Smith, Rose; Stowers, Yvette; Suero-Gabler, Cynthia; Thomas, Robert; Torres, Rodrigo; Torres, Rodrigo; Tran, Mai (Legal); Treichelt, Tim; Vasquez, Rosalyn; Vasquez, Rosalyn; Wallentine, Sean; Whitaker, Lynn; Williams, Lee; Worley, Tabitha; Zivkovich, Robert
Subject: State Board of Equalization - Announcement of Regulatory Change 1618

The State Board of Equalization proposes to amend Sales and Use Tax Regulation 1618, *United States Government Supply Contracts*. A public hearing regarding the proposed amendments will be held in Room 121, 450 N Street, Sacramento, at 9:30 a.m., or as soon thereafter as the matter may be heard, on Tuesday, June 26, 2012.

The proposed amendments make the regulation consistent with the Federal Acquisition Regulation (FAR) and clarify the requirements for sales for resale to the United States.

To view the notice of proposed regulatory action, initial statement of reasons, proposed text, and history click on the following link:
http://www.boe.ca.gov/regs/reg_1618_2012.htm.

Questions regarding the substance of the proposed amendments should be directed to Mr. Bradley Heller, Tax Counsel IV, at 450 N Street, MIC:82, Sacramento, CA 94279-0082, email Bradley.Heller@boe.ca.gov, telephone (916) 323-3091, or FAX (916) 323-3387.

Written comments for the Board's consideration, notices of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed regulatory action should be directed to Mr. Rick Bennion, Regulations Coordinator, telephone (916) 445-2130, fax (916) 324-3984, e-mail Richard.Bennion@boe.ca.gov or by mail to: State Board of Equalization, Attn: Rick Bennion, MIC: 80, P.O. Box 942879-0080, Sacramento, CA 94279-0080.

Please do not reply to this message.

Board Proceedings Division, MIC:80
Rick Bennion
Regulations Coordinator
Phone (916) 445-2130
Fax (916) 324-3984
Richard.Bennion@boe.ca.gov

Bennion, Richard

From: State Board of Equalization - Announcement of Regulatory Change
Sent: Friday, April 06, 2012 9:46 AM
To: 'BOE_REGULATIONS@listserv.state.ca.gov'
Subject: State Board of Equalization - Announcement of Regulatory Change 1684

The State Board of Equalization proposes to amend Sales and Use Tax Regulation 1684, *Collection of Use Tax by Retailers*. A public hearing regarding the proposed amendments will be held in Room 121, 450 N Street, Sacramento, at 9:30 a.m., or as soon thereafter as the matter may be heard, on Wednesday, May 30, 2012.

The proposed amendments make the regulation consistent with, clarify, and implement the amendments made to Revenue and Taxation Code section 6203 by AB 155 (Stats. 2011, ch. 313), which changed the definition of "retailer engaged in business in this state."

To view the notice of proposed regulatory action, initial statement of reasons, proposed text, and history click on the following link: http://www.boe.ca.gov/regs/reg_1684_2012.htm.

Questions regarding the substance of the proposed amendments should be directed to Mr. Bradley Heller, Tax Counsel IV, at 450 N Street, MIC:82, Sacramento, CA 94279-0082, email Bradley.Heller@boe.ca.gov, telephone (916) 323-3091, or FAX (916) 323-3387.

Written comments for the Board's consideration, notices of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed regulatory action should be directed to Mr. Rick Bennion, Regulations Coordinator, telephone (916) 445-2130, fax (916) 324-3984, e-mail Richard.Bennion@boe.ca.gov or by mail to: State Board of Equalization, Attn: Rick Bennion, MIC: 80, P.O. Box 942879-0080, Sacramento, CA 94279-0080.

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RESULTS OF THE ECONOMIC
IMPACT ANALYSIS

The proposed regulations:

- Will not result in the creation or elimination of jobs within the State of California;
- Will not result in the creation of new businesses or the elimination of existing businesses within the State of California;
- Will not result in the expansion of businesses currently doing business within the State of California.
- Will provide benefits to the health and welfare of California residents, worker safety, and the state's environment, by requiring the appropriate tug escorts for vessels calling at Los Angeles and Long Beach harbors, to potentially assist in the event of a propulsion or steering failure.

CONSIDERATION OF ALTERNATIVES

OSPR must determine that no reasonable alternative considered by OSPR or that has otherwise been identified and brought to the attention of OSPR would be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law.

AVAILABILITY OF DOCUMENTS AND OSPR
CONTACT PERSON

OSPR has prepared an Initial Statement of Reasons for the proposed regulatory action and has available all the information upon which the proposal is based. Copies of the exact language of the proposed regulations, Initial Statement of Reasons, the rulemaking file, the Final Statement of Reasons (when available) and other information, if any, may be obtained upon request from the:

Department of Fish and Game
Office of Spill Prevention and Response
P.O. Box 944209
Sacramento, California 94244-2090

In addition, the Notice, the exact language of the proposed regulations, and the Initial Statement of Reasons may be found on the World Wide Web at the following address:

http://www.dfg.ca.gov/ospr/Law/regs_under_review.asp

Questions regarding the proposed regulations, requests for documents, or any questions concerning the substance of this regulatory action may be directed to Joy Lavin-Jones ((916) 327-0910), or Mike Coyne ((916) 324-5659).

**TITLE 18. STATE BOARD OF
EQUALIZATION**

**Amendments to California Code of Regulations,
Title 18, Section 1618, *United States Government
Supply Contracts***

NOTICE IS HEREBY GIVEN

The State Board of Equalization (Board), pursuant to the authority vested in it by Revenue and Taxation Code (RTC) section 7051, proposes to adopt amendments to California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*. Regulation 1618 implements, interprets, and makes specific RTC section 6207, which provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business," and RTC section 6381, which provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States. The proposed amendments make the regulation consistent with the 2007 amendments to the Federal Acquisition Regulation (FAR) codified in chapter 1 of title 48 of the Code of Federal Regulations, and clarify the requirements for making sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 26-28, 2012. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at www.boe.ca.gov at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 9:30 a.m. or as soon thereafter as the matter may be heard on June 26, 27, or 28, 2012. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1618.

AUTHORITY

RTC section 7051.

REFERENCE

RTC sections 6007 and 6381.

INFORMATIVE DIGEST/POLICY STATEMENT
OVERVIEW

Current Regulation 1618

Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, RTC section 6007 provides that the term “retail sale” means “a sale for any purpose other than resale in the regular course of business” and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

Regulation 1618 currently prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor’s business (hereafter, “sales for resale to the United States”). The regulation generally provides that:

- A retailer’s sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer’s sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

Regulation 1618 also currently provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its

executive agencies, which are codified in the FAR, and Regulation 1618 provides specific guidance as to when title to “special tooling” passes to the United States under the FAR.

2007 Amendments to FAR

Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal’s decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to “special tooling” passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for “special tooling,” and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007.

Effect, Objectives, and Benefits of the Proposed Amendments to Regulation 1618

The Board directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts. At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR, and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term “tools,” as used in the definition of direct consumable supplies, does not include “special tooling”;
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term “tools,” as used in the definition of direct consumable supplies, includes “special tooling” that “was previously covered by FAR part 52.245-17”; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR’s title passage clauses for special tooling applied until June 13, 2007, but were no longer effective after that date.

In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for “overhead materials” must be allocated to United States Government supply contracts “consistent with government cost accounting standards.” It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to “direct consumable supplies” and “overhead materials” by separating sub-

division (b) into paragraphs (1) through (3), explaining that overhead materials are one example of “indirect consumable supplies,” and providing distinct guidance regarding the passage of title to direct consumable supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

The Aerospace Industries Association (AIA) participated in Board staff’s meetings with the interested parties and AIA agreed with staff’s recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

During its March 20, 2012, Business Taxes Committee meeting, the Board determined that staff’s recommended amendments are reasonably necessary to accomplish the objectives of making Regulation 1618 consistent with the 2007 amendments to the FAR and clarify Regulation 1618’s guidance regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials. The proposed amendments are anticipated to provide the following specific benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1618 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1618 is the only state regulation prescribing the requirements for making sales for resale to the United States. In addition, there is no federal sales tax and there are no comparable federal regulations or statutes to Regulation 1618.

NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

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

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The proposed amendments to Regulation 1618 make the regulation consistent with the 2007 amendments to the FAR, eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR, and provide more clarity and certainty regarding the requirements for sales for resale of direct consumable supplies and indirect consumable supplies, including overhead materials, to the United States. The proposed amendments were the result of a collaborative effort between Board staff and the interested parties and are intended to provide additional certainty to retailers. Furthermore, the proposed amendments will not impose any new taxes. Therefore, the Board has made an initial determination that the adoption of the proposed amendments to Regulation 1618 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulation 1618 may affect small business.

NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

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

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

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1618 will nei-

ther create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulation 1618 will not affect the health and welfare of California residents, worker safety, or the state's environment.

NO SIGNIFICANT EFFECT ON HOUSING COSTS

Adoption of the proposed amendments to Regulation 1618 will not have a significant effect on housing costs.

DETERMINATION REGARDING ALTERNATIVES

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

CONTACT PERSONS

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at Bradley.Heller@boe.ca.gov, or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at Richard.Bennion@boe.ca.gov, or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

WRITTEN COMMENT PERIOD

The written comment period ends at 9:30 a.m. on June 26, 2012, or as soon thereafter as the Board begins

the public hearing regarding the proposed amendments to Regulation 1684 during the June 26-28, 2012, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1618. The Board will only consider written comments received by that time.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared an underscored and strikeout version of the text of Regulation 1618 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rule-making file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at www.boe.ca.gov.

SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The Board may adopt the proposed amendments to Regulation 1618 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed amendments, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

AVAILABILITY OF FINAL STATEMENT
OF REASONS

If the Board adopts the proposed amendments to Regulation 1618, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at www.boe.ca.gov.

GENERAL PUBLIC INTEREST

DEPARTMENT OF FISH AND GAME

PROPOSED RESEARCH ON FULLY
PROTECTED SPECIES

Breeding Population Studies of the
California Least Tern

The Department of Fish and Game (Department) reviewed a proposal on April 5, 2012, from Michael Evans, National City, CA, requesting authorization to take the California least tern (*Sternula antillarum browni*), Fully Protected bird, for research purposes, consistent with protection and recovery of the species in San Diego, Orange, Los Angeles, and Ventura Counties.

The applicant is in the process of obtaining the required Scientific Collecting Permit (SCP) to take protected species of wildlife. Permit conditions require that the holder of an SCP obtain special authorization from the Department for research on Fully Protected species. The proposed activities include approaching least tern nesting areas to gather necessary data used in monitoring nesting status, conducting habitat assessments, and identifying threats. Data would be collected by observation and monitoring with binoculars/spotting scopes in or near potential and known breeding habitat and locating nests on foot. The Department intends to issue, under specified conditions, a Memorandum of Understanding (MOU) that would authorize the applicant to carry out the proposed activities. As these birds are also federally-listed endangered species, applicants are required to possess a valid Federal Threatened and Endangered Species permit.

Pursuant to California Fish and Game Code (FGC) Section 3511(a)(1), the Department may authorize take of Fully Protected birds after 30 days' notice has been provided to affected and interested parties through publication of this notice. If the Department determines that the proposed research is consistent with the requirements of FGC Section 3511 for take of Fully Protected birds, it would issue the authorization on or after May

20, 2012, for an initial and renewable term of two years. Contact: California Department of Fish and Game, Wildlife Branch, 1812 9th Street, Sacramento, CA 95811, Attn.: Esther Burkett.

DEPARTMENT OF FISH AND GAME

**CALIFORNIA ENDANGERED SPECIES ACT
CONSISTENCY DETERMINATION NO.
2080-2012-003-03**

Project: South Bay Aqueduct Improvement and
Enlargement Project

Location: Alameda County

Applicant: California Department of Water
Resources

Notifier: Jim O'Toole, Environmental Science
Associates

Background

The Department of Water Resources (DWR) (Applicant) proposes to improve and enlarge the South Bay Aqueduct (SBA) System. The SBA Improvement and Enlargement Project (Project) includes the following elements:

- Bethany Reservoir facility improvements including expansion of an existing building, the installation of additional pumps, a new service bay and a new electrical switchyard at the South Bay Pumping Plant (SBPP) on Bethany Reservoir, and SBPP inlet dredging;
- Construction of a third parallel Brushy Creek pipeline and surge tank parallel to the existing dual pipeline system;
- Construction of the 27-acre Dyer Reservoir, a 500-acre-foot capacity reservoir to be served by the Stage 3 Brushy Creek Pipeline;
- Development of the first phase of a water pipeline from Dyer Reservoir to the proposed Altamont Water Treatment Plant west of Dyer Road;
- Raising the height of canal embankments, canal lining and canal overcrossing structures and bridges for the Dyer, Livermore, and Alameda canals, including Patterson Reservoir, which includes use of the 17-acre Patterson embankment materials borrow area;
- Modification of check structures and siphons along the Dyer, Livermore, and Alameda canals; and
- Construction of new drainage overcrossing structures to eliminate drainage into canals.



STATE BOARD OF EQUALIZATION

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BETTY T. YEE
First District, San Francisco
SEN. GEORGE RUNNER (RET.)
Second District, Lancaster
MICHELLE STEEL
Third District, Rolling Hills Estates
JEROME E. HORTON
Fourth District, Los Angeles
JOHN CHIANG
State Controller
KRISTINE CAZADD
Executive Director

April 20, 2012

To Interested Parties:

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

**Proposed to Adopt Amendments to California Code of Regulations, Title 18,
Section 1618, *United States Government Supply Contracts***

NOTICE IS HEREBY GIVEN

The State Board of Equalization (Board), pursuant to the authority vested in it by Revenue and Taxation Code (RTC) section 7051, proposes to adopt amendments to California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*. Regulation 1618 implements, interprets, and makes specific RTC section 6207, which provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business," and RTC section 6381, which provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States. The proposed amendments make the regulation consistent with the 2007 amendments to the Federal Acquisition Regulation (FAR) codified in chapter 1 of title 48 of the Code of Federal Regulations, and clarify the requirements for making sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 26-28, 2012. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at www.boe.ca.gov at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 9:30 a.m. or as soon thereafter as the matter may be heard on June 26, 27, or 28, 2012. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1618.

AUTHORITY

RTC section 7051.

REFERENCE

RTC sections 6007 and 6381.

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

Current Regulation 1618

Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, RTC section 6007 provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business" and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

Regulation 1618 currently prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor's business (hereafter, "sales for resale to the United States"). The regulation generally provides that:

- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

Regulation 1618 also currently provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in the FAR, and Regulation 1618 provides specific guidance as to when title to "special tooling" passes to the United States under the FAR.

2007 Amendments to FAR

Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal's decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to "special tooling" passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for "special tooling," and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007.

Effect, Objectives, and Benefits of the Proposed Amendments to Regulation 1618

The Board directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts. At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR, and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term "tools," as used in the definition of direct consumable supplies, does not include "special tooling";
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term "tools," as used in the definition of direct consumable supplies, includes "special tooling" that "was previously covered by FAR part 52.245-17"; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR's title passage clauses for special tooling applied until Jun 13, 2007, but were no longer effective after that date.

In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for "overhead materials" must be allocated to United States Government supply contracts "consistent with government cost accounting standards." It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to "direct consumable supplies" and "overhead materials" by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of "indirect consumable supplies," and providing distinct guidance regarding the passage of title to direct consumable supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

The Aerospace Industries Association (AIA) participated in Board staff's meetings with the interested parties and AIA agreed with staff's recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

During its March 20, 2012, Business Taxes Committee meeting, the Board determined that staff's recommended amendments are reasonably necessary to accomplish the objectives of making Regulation 1618 consistent with the 2007 amendments to the FAR and clarifying Regulation 1618's guidance regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials. The proposed amendments are anticipated to provide the following specific benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1618 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1618 is the only state regulation prescribing the requirements for making sales for resale to the United States. In addition, there is no federal sales tax and there are no comparable federal regulations or statutes to Regulation 1618.

NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

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

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The proposed amendments to Regulation 1618 make the regulation consistent with the 2007 amendments to the FAR, eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR, and provide more clarity and certainty regarding the requirements

for sales for resale of direct consumable supplies and indirect consumable supplies, including overhead materials, to the United States. The proposed amendments were the result of a collaborative effort between Board staff and the interested parties and are intended to provide additional certainty to retailers. Furthermore, the proposed amendments will not impose any new taxes. Therefore, the Board has made an initial determination that the adoption of the proposed amendments to Regulation 1618 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulation 1618 may affect small business.

NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

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

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

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1618 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulation 1618 will not affect the health and welfare of California residents, worker safety, or the state's environment.

NO SIGNIFICANT EFFECT ON HOUSING COSTS

Adoption of the proposed amendments to Regulation 1618 will not have a significant effect on housing costs.

DETERMINATION REGARDING ALTERNATIVES

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

CONTACT PERSONS

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at Bradley.Heller@boe.ca.gov, or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at Richard.Bennion@boe.ca.gov, or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

WRITTEN COMMENT PERIOD

The written comment period ends at 9:30 a.m. on June 26, 2012, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulation 1684 during the June 26-28, 2012, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1618. The Board will only consider written comments received by that time.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared an underscored and strikeout version of the text of Regulation 1618 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at www.boe.ca.gov.

SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

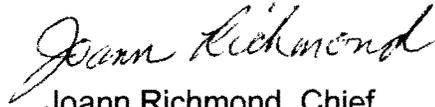
The Board may adopt the proposed amendments to Regulation 1618 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will

make the full text of the proposed amendments, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulation 1618, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at www.boe.ca.gov

Sincerely,


Joann Richmond, Chief
Board Proceedings Division

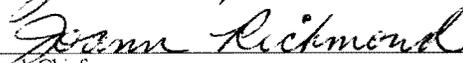
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STATE BOARD OF EQUALIZATION



BOARD APPROVED

At the June 26, 2012 Board Meeting


Joann Richmond, Chief
Board Proceedings Division

Initial Statement of Reasons

Adoption of Proposed Amendments to California Code of Regulations, Title 18, Section 1618, *United States Government Supply Contracts*

SPECIFIC PURPOSE AND NECESSITY

Regulation 1618

Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, Revenue and Taxation Code (RTC) section 6007 provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business" and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*, prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor's business (hereafter, "sales for resale to the United States"). The regulation generally provides that:

- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

Regulation 1618 also provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in chapter 1 of title 48 of the Code of Federal Regulations, the Federal Acquisition

Regulation (FAR); and Regulation 1618 provides specific guidance as to when title to “special tooling” passes to the United States under the FAR.

2007 Amendments to FAR

Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal’s decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to “special tooling” passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for “special tooling,” and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007. Therefore, the State Board of Equalization (Board) directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts.

At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR (the problem to be addressed for purposes of Government Code section 11346.2, subdivision (b)(1)), and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term “tools,” as used in the definition of direct consumable supplies, does not include “special tooling”;
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term “tools,” as used in the definition of direct consumable supplies, includes “special tooling” that “was previously covered by FAR part 52.245-17”; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR’s title passage clauses for special tooling applied until Jun 13, 2007, but were no longer effective after that date.

In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for “overhead materials” must be allocated to United States Government supply contracts “consistent with government cost accounting standards.” It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to “direct consumable supplies” and “overhead materials” by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of “indirect consumable supplies,” and providing distinct guidance regarding the passage of title to direct consumable supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

The Aerospace Industries Association (AIA) participated in Board staff's meetings with the interested parties and AIA agreed with staff's recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

Business Taxes Committee Meeting

The Board considered Formal Issue Paper 12-001 during its March 20, 2012, Business Taxes Committee meeting, and the Board unanimously voted to propose the adoption of staff's recommended amendments to Regulation 1618 because the Board determined that the amendments are reasonably necessary for the specific purposes of:

- Conforming Regulation 1618 to the 2007 amendments to the FAR, particularly the repeal of FAR part 52.245-17 regarding special tooling;
- Clarifying that costs for overhead materials must be allocated to United States Government supply contracts consistent with government cost accounting standards;
- Clarifying that overhead materials are one example of indirect consumable supplies; and
- Providing distinct guidance regarding the passage of title to direct consumable supplies and indirect consumable supplies, including overhead materials.

The proposed amendments are anticipated to provide the following benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

The proposed amendments to Regulation 1618 were not mandated by federal law or regulations, although changes to federal regulations are one of the reasons why the proposed amendments are necessary. There is no previously adopted or amended federal regulation that is identical to Regulation 1618.

DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 12-001, the exhibits to the formal issue paper, and the comments made during the Board's discussion of the formal issue paper during its March 20, 2012, Business Taxes Committee meeting in deciding to propose the amendments to Regulation 1618 described above.

ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulation 1618 at this time or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed amendments at this time because the Board determined that the amendments are reasonably necessary for the reasons set forth above.

The Board did not reject any reasonable alternative to the proposed amendments to Regulation 1618 that would lessen any adverse impact the proposed action may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed action. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2, SUBDIVISION (b)(6) AND ECONOMIC IMPACT ANALYSIS REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The proposed amendments to Regulation 1618 make the regulation consistent with the 2007 amendments to the FAR, eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR, and provide more clarity and certainty regarding the requirements for sales for resale of direct consumable supplies and indirect consumable supplies, including overhead materials, to the United States. The proposed amendments were the result of a collaborative effort between Board staff and the interested parties and are intended to provide additional certainty to retailers. In addition, the proposed amendments will not impose any new taxes. Therefore, the Board has determined that the adoption of the proposed amendments to Regulation 1618 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

Furthermore, Regulation 1618 does not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Board has also determined that the adoption of the proposed amendments to Regulation 1618 will not affect the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulation 1618 will not have a significant adverse economic impact on business.

The proposed amendments may affect small business.

**Text of Proposed Amendments to
California Code of Regulations, Title 18, Section 1618**

Section 1618. United States Government Supply Contracts.

(a) Definitions.

(1) "United States Government supply contract" means a contract with the United States to furnish, or to fabricate and furnish, tangible personal property including ships, aircraft, ordnance, or equipment, whereby title to tangible personal property purchased for use in fulfilling the contract passes to the United States pursuant to the title provisions contained in the contract before the contractor uses the property to perform the function or act for which the property was designed or manufactured. The term "U.S. Government supply contract" does not include contracts to construct improvements on or to real property or to the purchase of tangible personal property for use in fulfilling such contracts.

(2) "Direct consumable supplies" means supplies, tools, or equipment consumed in the performance of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~"Tools" as used in this definition does not include "special tooling" subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17. Effective June 14, 2007, "Tools" as used in this definition includes "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.~~

(3) "Overhead materials" means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

(2) Whether title to direct consumable supplies ~~and/or indirect consumable supplies~~ (i.e., overhead materials) passes to the United States under a United States government supply contract and the time at which title passes will be determined in

accordance with the title provisions contained in the contract, if any. ~~In a case where the cost of~~

(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

(B) F-or indirect consumable supplies (i.e., overhead materials), which are charged to an expense account which is then allocated to various locations, cost centers or contracts, ~~some of which are engaged in other than United States government cost reimbursement contracts and/or fixed price contracts with a progress payments clause,~~ it will be considered that title ~~did not pass~~ to the United States government prior to use of the property, and tax will not apply with respect to the purchase or use of the property charged to the expense account, ~~unless~~ if the item is ~~specifically accounted for as being charged~~ allocated to a specific United States government supply contract, pursuant to the terms of which title passes to the United States prior to the use of the item. Property will be considered ~~charged~~ allocated to a specific United States government supply contract when it is allocated pursuant to:

(1)-a1. Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,

(2)-g2. Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in ~~this~~ the manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

(3) Special Tooling. Effective December 29, 1989 through June 13, 2007, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17. Title to such special tooling will pass prior to use by the contractor only if the agreement between the contractor and the United States government contains a custom clause providing for title passage prior to use by the contractor. Therefore, sales of special tooling will generally be subject to tax.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6007 and 6381, Revenue and Taxation Code; and Aerospace Corp. v. St. Bd. of Equalization (1990) 218 Cal.App.3d 1300.

Regulation History

Type of Regulation: Sales and Use Tax

Regulation: 1618

Title: 1618, *United States Government Supply Contracts*

Preparation: Brad Heller

Legal Contact: Brad Heller

Board proposes to amend Regulation 1618, *United States Government Supply Contracts*, to make the regulation consistent with the Federal Acquisition Regulation (FAR) and clarify the requirements for sales for resale to the United States.

History of Proposed Regulation:

June 26-28, 2012	Public Hearing
April 20, 2012	OAL publication date; 45-day public comment period begins; Interested Parties mailing
April 6, 2012	Notice to OAL
March 20, 2012	Business Tax Committee, Board Authorized Publication (Vote 5-0)

Sponsor:	NA
Support:	NA
Oppose:	NA

Statement of Compliance

The State Board of Equalization, in process of adopting Special Taxes Regulation 1618, *United States Government Supply Contracts*, did comply with the provision of Government Code section 11346.4(a)(1) through (4). A notice to interested parties was mailed on April 20, 2012, 67 days prior to the public hearing.

May 2, 2012

A handwritten signature in black ink, appearing to read "Richard Bennion", written over a horizontal line.

Richard Bennion
Regulations Coordinator
State Board of Equalization

BEFORE THE CALIFORNIA STATE BOARD OF EQUALIZATION

450 N STREET

SACRAMENTO, CALIFORNIA

REPORTER'S TRANSCRIPT

JUNE 26, 2012

ITEM F PUBLIC HEARINGS

ITEM F3

PROPOSED ADOPTION OF AMENDMENTS TO REGULATION 1618,
UNITED STATES GOVERNMENT SUPPLY CONTRACTS

REPORTED BY: Kathleen Skidgel

CSR NO. 9039

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 the Board:

Bradley Heller
Tax Counsel IV
Legal Department

---oOo---

1 450 N STREET
2 SACRAMENTO, CALIFORNIA
3 JUNE 26, 2012

4 ----oOo----

5 MR. HORTON: Ms. Richmond.

6 MS. RICHMOND: Our next item is F3, Proposed
7 Adoption of Amendments to Regulation 1618, United States
8 Government Supply Contracts.

9 MR. HELLER: Good afternoon, Chairman Horton.

10 MR. HORTON: Good afternoon, young man. How
11 are you?

12 MR. HELLER: I'm very good. How are you?

13 MR. HORTON: Good. Welcome to the Board.

14 MR. HELLER: Thank you.

15 Board Members, um, I'm Bradley Heller from the
16 Board's Legal Department.

17 I'm here to request that the Board, uh, vote to
18 adopt the proposed amendments to Regulation 1618, United
19 States Government Supply Contractors which the Board
20 authorized for publication back in March.

21 The proposed amendments make the regulation
22 consistent with 2007 amendments to the Federal
23 Acquisition Regulation and clarify the requirements for
24 making sales for resale to the United States Government
25 of direct consumable supplies and indirect consumable
26 supplies -- excuse me, indirect consumable supplies,
27 including overhead materials.

28 Uh, the proposed amendments were the result of

1 a cooperative interested parties process between staff
2 and industry.

3 I can answer any questions you might have.

4 MR. HORTON: Discussion, Members?

5 Is there --

6 MS. YEE: Move adoption.

7 MR. HORTON: -- a motion?

8 MS. STEEL: So move.

9 MR. HORTON: Move adoption by Member Yee.

10 Second by Member Steel.

11 Without objection, such will be the order.

12 Thank you again.

13 MR. HELLER: Thank you.

14 MR. HORTON: Uh, appreciate it. Codifying a
15 solution, that's a good thing. Appreciate it.

16 ----oOo----

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REPORTER'S CERTIFICATE

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State of California)
) ss
County of Sacramento)

I, KATHLEEN SKIDGEL, Hearing Reporter for the California State Board of Equalization certify that on June 26, 2012 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: July 3, 2012

Kathleen Skidgel



KATHLEEN SKIDGEL, CSR #9039
Hearing Reporter

2012 MINUTES OF THE STATE BOARD OF EQUALIZATION**Tuesday, June 26, 2012**

Speakers: Jesse W. McClellan, Partner, McClellan Davis LLC, Associated Sales Tax Consultants
Myron Sidie, President, Faces, Inc.

F2 Property Taxpayers' Bill of Rights Hearings

Todd Gilman, Chief, Taxpayers' Rights and Equal Employment Opportunity Division, made introductory remarks regarding the Property Taxpayers' Bill of Rights hearings. Individuals have the opportunity to present their ideas, concerns, and recommendations regarding legislation, the quality of agency services, and other issues related to the Board's administration of its tax programs, including state and county property tax programs, and any problems identified in the Taxpayers' Rights Advocate's Annual Report.

Speakers: Joel Butler, Yolo County Assessor
Kathleen Kelleher, Sacramento County Assessor

F3 Proposed adoption of amendments to Regulation 1618, *United States Government Supply Contracts*

Bradley Heller, Tax Counsel, Tax and Fee Program Division, Legal Department, made introductory remarks regarding staff's request for adoption of the proposed amendments to regulation to Regulation 1618, which make the regulation consistent with the Federal Acquisition Regulation (FAR) and clarify the requirements for sales for resale to the United States (Exhibit 6.2).

Speakers were invited to address the Board, but there were none.

Action: Upon motion of Ms. Yee, seconded by Ms. Steel and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee, Mr. Runner and Ms. Mandel voting yes, the Board adopted the proposed amendments as recommended by staff.

[G1] LEGAL APPEALS MATTERS, CONSENT

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

G1.1 Kingdom Holdings, LLC, 464450, 535888 (EA)
2-1-05 to 12-31-07, \$12,177.82 Tax

Action: No adjustment be made in the administrative protest and the claim for refund be denied as recommended by the Appeals Division.



STATE BOARD OF EQUALIZATION
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BETTY T. YEE
First District, San Francisco

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

MICHELLE STEEL
Third District, Rolling Hills Estates

JEROME E. HORTON
Fourth District, Los Angeles

JOHN CHIANG
State Controller

KRISTINE CAZADD
Executive Director

April 20, 2012

To Interested Parties:

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

**Proposed to Adopt Amendments to California Code of Regulations, Title 18,
Section 1618, *United States Government Supply Contracts***

NOTICE IS HEREBY GIVEN

The State Board of Equalization (Board), pursuant to the authority vested in it by Revenue and Taxation Code (RTC) section 7051, proposes to adopt amendments to California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*. Regulation 1618 implements, interprets, and makes specific RTC section 6207, which provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business," and RTC section 6381, which provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States. The proposed amendments make the regulation consistent with the 2007 amendments to the Federal Acquisition Regulation (FAR) codified in chapter 1 of title 48 of the Code of Federal Regulations, and clarify the requirements for making sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on June 26-28, 2012. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at www.boe.ca.gov at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 9:30 a.m. or as soon thereafter as the matter may be heard on June 26, 27, or 28, 2012. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1618.

AUTHORITY

RTC section 7051.

REFERENCE

RTC sections 6007 and 6381.

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

Current Regulation 1618

Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, RTC section 6007 provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business" and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

Regulation 1618 currently prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor's business (hereafter, "sales for resale to the United States"). The regulation generally provides that:

- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

Regulation 1618 also currently provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in the FAR, and Regulation 1618 provides specific guidance as to when title to "special tooling" passes to the United States under the FAR.

2007 Amendments to FAR

Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal's decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to "special tooling" passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for "special tooling," and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007.

Effect, Objectives, and Benefits of the Proposed Amendments to Regulation 1618

The Board directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts. At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR, and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term "tools," as used in the definition of direct consumable supplies, does not include "special tooling";
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term "tools," as used in the definition of direct consumable supplies, includes "special tooling" that "was previously covered by FAR part 52.245-17"; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR's title passage clauses for special tooling applied until Jun 13, 2007, but were no longer effective after that date.

In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for "overhead materials" must be allocated to United States Government supply contracts "consistent with government cost accounting standards." It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to "direct consumable supplies" and "overhead materials" by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of "indirect consumable supplies," and providing distinct guidance regarding the passage of title to direct consumable supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

The Aerospace Industries Association (AIA) participated in Board staff's meetings with the interested parties and AIA agreed with staff's recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

During its March 20, 2012, Business Taxes Committee meeting, the Board determined that staff's recommended amendments are reasonably necessary to accomplish the objectives of making Regulation 1618 consistent with the 2007 amendments to the FAR and clarifying Regulation 1618's guidance regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials. The proposed amendments are anticipated to provide the following specific benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1618 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1618 is the only state regulation prescribing the requirements for making sales for resale to the United States. In addition, there is no federal sales tax and there are no comparable federal regulations or statutes to Regulation 1618.

NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will not impose a mandate on local agencies or school districts, including a mandate that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

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

The Board has determined that the adoption of the proposed amendments to Regulation 1618 will result in no direct or indirect cost or savings to any state agency, any cost to local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The proposed amendments to Regulation 1618 make the regulation consistent with the 2007 amendments to the FAR, eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR, and provide more clarity and certainty regarding the requirements

for sales for resale of direct consumable supplies and indirect consumable supplies, including overhead materials, to the United States. The proposed amendments were the result of a collaborative effort between Board staff and the interested parties and are intended to provide additional certainty to retailers. Furthermore, the proposed amendments will not impose any new taxes. Therefore, the Board has made an initial determination that the adoption of the proposed amendments to Regulation 1618 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulation 1618 may affect small business.

NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

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

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

The Board has prepared the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1618 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California. Furthermore, the Board has determined that the adoption of the proposed amendments to Regulation 1618 will not affect the health and welfare of California residents, worker safety, or the state's environment.

NO SIGNIFICANT EFFECT ON HOUSING COSTS

Adoption of the proposed amendments to Regulation 1618 will not have a significant effect on housing costs.

DETERMINATION REGARDING ALTERNATIVES

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

CONTACT PERSONS

Questions regarding the substance of the proposed amendments should be directed to Bradley M. Heller, Tax Counsel IV, by telephone at (916) 323-3091, by e-mail at Bradley.Heller@boe.ca.gov, or by mail at State Board of Equalization, Attn: Bradley M. Heller, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the Board's consideration, notice of intent to present testimony or witnesses at the public hearing, and inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 324-3984, by e-mail at Richard.Bennion@boe.ca.gov, or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

WRITTEN COMMENT PERIOD

The written comment period ends at 9:30 a.m. on June 26, 2012, or as soon thereafter as the Board begins the public hearing regarding the proposed amendments to Regulation 1684 during the June 26-28, 2012, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1618. The Board will only consider written comments received by that time.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The Board has prepared an underscored and strikeout version of the text of Regulation 1618 illustrating the express terms of the proposed amendments and an initial statement of reasons for the adoption of the proposed amendments, which includes the economic impact analysis required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at www.boe.ca.gov.

SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The Board may adopt the proposed amendments to Regulation 1618 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will

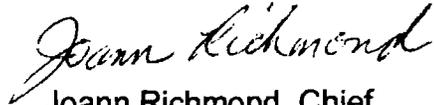
April 20, 2012

make the full text of the proposed amendments, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting amendments will be mailed to those interested parties who commented on the original proposed amendments orally or in writing or who asked to be informed of such changes. The text of the resulting amendments will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting amendments that are received prior to adoption.

AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulation 1618, the Board will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the Board's Website at www.boe.ca.gov

Sincerely,


Joann Richmond, Chief
Board Proceedings Division

JR:reb

Initial Statement of Reasons
Adoption of Proposed Amendments to
California Code of Regulations, Title 18, Section 1618,
United States Government Supply Contracts

SPECIFIC PURPOSE AND NECESSITY

Regulation 1618

Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, Revenue and Taxation Code (RTC) section 6007 provides that the term "retail sale" means "a sale for any purpose other than resale in the regular course of business" and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*, prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor's business (hereafter, "sales for resale to the United States"). The regulation generally provides that:

- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer's sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

Regulation 1618 also provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in chapter 1 of title 48 of the Code of Federal Regulations, the Federal Acquisition

Regulation (FAR); and Regulation 1618 provides specific guidance as to when title to “special tooling” passes to the United States under the FAR.

2007 Amendments to FAR

Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal’s decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to “special tooling” passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for “special tooling,” and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007. Therefore, the State Board of Equalization (Board) directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts.

At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR (the problem to be addressed for purposes of Government Code section 11346.2, subdivision (b)(1)), and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term “tools,” as used in the definition of direct consumable supplies, does not include “special tooling”;
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term “tools,” as used in the definition of direct consumable supplies, includes “special tooling” that “was previously covered by FAR part 52.245-17”; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR’s title passage clauses for special tooling applied until Jun 13, 2007, but were no longer effective after that date.

In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for “overhead materials” must be allocated to United States Government supply contracts “consistent with government cost accounting standards.” It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to “direct consumable supplies” and “overhead materials” by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of “indirect consumable supplies,” and providing distinct guidance regarding the passage of title to direct consumable supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

The Aerospace Industries Association (AIA) participated in Board staff's meetings with the interested parties and AIA agreed with staff's recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

Business Taxes Committee Meeting

The Board considered Formal Issue Paper 12-001 during its March 20, 2012, Business Taxes Committee meeting, and the Board unanimously voted to propose the adoption of staff's recommended amendments to Regulation 1618 because the Board determined that the amendments are reasonably necessary for the specific purposes of:

- Conforming Regulation 1618 to the 2007 amendments to the FAR, particularly the repeal of FAR part 52.245-17 regarding special tooling;
- Clarifying that costs for overhead materials must be allocated to United States Government supply contracts consistent with government cost accounting standards;
- Clarifying that overhead materials are one example of indirect consumable supplies; and
- Providing distinct guidance regarding the passage of title to direct consumable supplies and indirect consumable supplies, including overhead materials.

The proposed amendments are anticipated to provide the following benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

The proposed amendments to Regulation 1618 were not mandated by federal law or regulations, although changes to federal regulations are one of the reasons why the proposed amendments are necessary. There is no previously adopted or amended federal regulation that is identical to Regulation 1618.

DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 12-001, the exhibits to the formal issue paper, and the comments made during the Board's discussion of the formal issue paper during its March 20, 2012, Business Taxes Committee meeting in deciding to propose the amendments to Regulation 1618 described above.

ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulation 1618 at this time or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed amendments at this time because the Board determined that the amendments are reasonably necessary for the reasons set forth above.

The Board did not reject any reasonable alternative to the proposed amendments to Regulation 1618 that would lessen any adverse impact the proposed action may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed action. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2, SUBDIVISION (b)(6) AND ECONOMIC IMPACT ANALYSIS REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The proposed amendments to Regulation 1618 make the regulation consistent with the 2007 amendments to the FAR, eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR, and provide more clarity and certainty regarding the requirements for sales for resale of direct consumable supplies and indirect consumable supplies, including overhead materials, to the United States. The proposed amendments were the result of a collaborative effort between Board staff and the interested parties and are intended to provide additional certainty to retailers. In addition, the proposed amendments will not impose any new taxes. Therefore, the Board has determined that the adoption of the proposed amendments to Regulation 1618 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

Furthermore, Regulation 1618 does not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Board has also determined that the adoption of the proposed amendments to Regulation 1618 will not affect the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulation 1618 will not have a significant adverse economic impact on business.

The proposed amendments may affect small business.

**Text of Proposed Amendments to
California Code of Regulations, Title 18, Section 1618**

Section 1618. United States Government Supply Contracts.

(a) Definitions.

(1) "United States Government supply contract" means a contract with the United States to furnish, or to fabricate and furnish, tangible personal property including ships, aircraft, ordnance, or equipment, whereby title to tangible personal property purchased for use in fulfilling the contract passes to the United States pursuant to the title provisions contained in the contract before the contractor uses the property to perform the function or act for which the property was designed or manufactured. The term "U.S. Government supply contract" does not include contracts to construct improvements on or to real property or to the purchase of tangible personal property for use in fulfilling such contracts.

(2) "Direct consumable supplies" means supplies, tools, or equipment consumed in the performance of a contract which are specifically identified to the contract and the actual cost of which is charged as a direct item of cost to the specific contract. ~~"Tools" as used in this definition does not include "special tooling" subject to the provisions of Federal Acquisition Regulation (FAR) 52.245-17 or any regulation(s) which succeeds FAR 52.245-17.~~ Effective June 14, 2007, "Tools" as used in this definition includes "special tooling" that was previously covered by Federal Acquisition Regulation (FAR) 52.245-17.

(3) "Overhead materials" means supplies consumed in the performance of a contract the cost of which is charged to an overhead expense account and then allocated to various contracts based on generally accepted accounting principles and consistent with government cost accounting standards.

(b) Application of Tax.

(1) Sales to U.S. Government supply contractors of tools, equipment, direct consumable supplies and overhead materials are sales for resale if the United States takes title pursuant to a United States government supply contract prior to any use of the property by the contractor to perform the function or act for which the property was designed or manufactured. Accordingly, tax does not apply to such sales even though the property does not become a component part of the tangible personal property furnished, fabricated, or manufactured by the contractor. If the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the passage of title to the United States, tax applies to the sales to or to the use by the contractor.

(2) Whether title to direct consumable supplies ~~and~~ or indirect consumable supplies (i.e., overhead materials) passes to the United States under a United States government supply contract and the time at which title passes will be determined in

accordance with the title provisions contained in the contract, if any. ~~In a case where the cost of~~

(A) For direct consumable supplies, which are charged direct to the United States government contract, title passes to the United States government pursuant to the title passage clause(s) associated with that specific contract.

(B) For indirect consumable supplies (i.e., overhead materials), which are charged to an expense account which is then allocated to various locations, cost centers or contracts, ~~some of which are engaged in other than United States government cost reimbursement contracts and/or fixed price contracts with a progress payments clause,~~ it will be considered that title ~~did not pass~~ to the United States government prior to use of the property, and tax will not apply with respect to the purchase or use of the property charged to the expense account, unless the item is specifically accounted for as being charged/allocated to a specific United States government supply contract, pursuant to the terms of which title passes to the United States prior to the use of the item. Property will be considered charged/allocated to a specific United States government supply contract when it is allocated pursuant to:

~~(1)-a1.~~ Accounting standards promulgated by the Cost Accounting Standards Board (Office of Federal Procurement Policy, Office of Management and Budget), if applicable; otherwise,

~~(2)-g2.~~ Generally accepted accounting principles that are equitable, consistently-applied, and appropriate to the particular circumstances.

Direct consumable supplies identified in subdivision (b)(2)(A) and indirect consumable supplies (i.e., overhead materials) which may be allocated in ~~this~~ the manner identified in subdivision (b)(2)(B) include, but are not limited to, property used to repair items of capital equipment when a portion of the contractor's use is properly allocable to its government supply contracts, notwithstanding the fact that title to the property being repaired remains with the contractor.

(3) Special Tooling. Effective December 29, 1989 through June 13, 2007, title will generally not pass prior to use by the contractor for special tooling which is subject to the Special Tooling Clauses of Federal Acquisition Regulation (48 CFR) 52.245-17. Title to such special tooling will pass prior to use by the contractor only if the agreement between the contractor and the United States government contains a custom clause providing for title passage prior to use by the contractor. Therefore, sales of special tooling will generally be subject to tax.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6007 and 6381, Revenue and Taxation Code; and Aerospace Corp. v. St. Bd. of Equalization (1990) 218 Cal.App.3d 1300.

Regulation History

Type of Regulation: Sales and Use Tax

Regulation: 1618

Title: 1618, *United States Government Supply Contracts*

Preparation: Brad Heller

Legal Contact: Brad Heller

Board proposes to amend Regulation 1618, *United States Government Supply Contracts*, to make the regulation consistent with the Federal Acquisition Regulation (FAR) and clarify the requirements for sales for resale to the United States.

History of Proposed Regulation:

June 26-28, 2012	Public Hearing
April 20, 2012	OAL publication date; 45-day public comment period begins; Interested Parties mailing
April 6, 2012	Notice to OAL
March 20, 2012	Business Tax Committee, Board Authorized Publication (Vote 5-0)

Sponsor:	NA
Support:	NA
Oppose:	NA