

Rulemaking File  
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Sales and Use Tax

Regulation 1655, *Returns, Defects and Replacements*

*OAL Approval*

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**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 *JO*  
DATE: 6/11/2014  
RE: Return of Approved Rulemaking Materials  
OAL File No. 2014-0509-02S

OAL hereby returns this file your agency submitted for our review (OAL File No. 2014-0509-02S regarding Returns, Defects and Replacements).

Enclosures 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 regulation is specified on the Form 400 (see item B.5). **Beginning January 1, 2013**, unless an exemption applies, Government Code section 11343.4 states the effective date of an approved regulation is determined by the date the regulation is filed with the Secretary of State (see the date the Form 400 was stamped "ENDORSED FILED" by the Secretary of State) as follows:

- (1) **January 1** if the regulation or order of repeal is filed on September 1 to November 30, inclusive.
- (2) **April 1** if the regulation or order of repeal is filed on December 1 to February 29, inclusive.
- (3) **July 1** if the regulation or order of repeal is filed on March 1 to May 31, inclusive.
- (4) **October 1** if the regulation or order of repeal is filed on June 1 to August 31, inclusive.

If an exemption applies concerning the effective date of the regulation approved in this file, then it will be specified on the Form 400. The Notice of Approval that OAL sends to the state agency will contain the effective date of the regulation. The history note that will appear at the end of the regulation section in the California Code of Regulations will also include the regulation's effective date. Additionally, the effective date of the regulation will be noted on OAL's Web site once OAL posts the Internet Web site link to the full text of the regulation that is received from the state agency. (Gov. Code, secs. 11343 and 11344.)

**Please note this new requirement:** Unless an exemption applies, Government Code section 11343 now requires:

1. **Section 11343(c)(1):** Within 15 days of OAL filing a state agency's regulation with the Secretary of State, the state agency is required to post the regulation on its Internet Web site in an easily marked and identifiable location. The state agency shall keep the regulation posted on its Internet Web site for at least six months from the date the regulation is filed with the Secretary of State.
2. **Section 11343(c)(2):** Within five (5) days of posting its regulation on its Internet Web site, the state agency shall send to OAL the Internet Web site link of each regulation that the agency posts on its Internet Web site pursuant to section 11343(c)(1).

OAL has established an email address for state agencies to send the Internet Web site link to for each regulation the agency posts. Please send the Internet Web site link for each regulation posted to OAL at [postedregslink@oal.ca.gov](mailto:postedregslink@oal.ca.gov).

**NOTE ABOUT EXEMPTIONS.** Posting and linking requirements do not apply to emergency regulations; regulations adopted by FPPC or Conflict of Interest regulations approved by FPPC; and regulations not subject to OAL/APA review. However, an exempt agency may choose to comply with these requirements, and OAL will post the information accordingly.

**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 State 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

RECEIVED

JUN 13 2014

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:

Government Code Section 11349.3

Title 18, California Code of Regulations

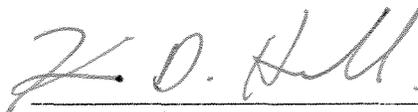
OAL File No. 2014-0509-02 S

Adopt sections:  
Amend sections: 1655  
Repeal sections:

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

OAL approves this regulatory action pursuant to section 11349.3 of the Government Code. This regulatory action becomes effective on 10/1/2014.

Date: 6/11/2014



Kevin D. Hull  
Senior Attorney

For: DEBRA M. CORNEZ  
Director

Original: Cynthia Bridges  
Copy: Richard Bennion

## NOTICE PUBLICATION/REGULATIONS SUBMISSION

**REGULAR**

(See instructions on reverse)

For use by Secretary of State only

STD. 400 (REV. 01-2013)

OAL FILE NUMBERS	NOTICE FILE NUMBER <b>Z-14-0204-03</b>	REGULATORY ACTION NUMBER <b>2014-0509-025</b>	EMERGENCY NUMBER
For use by Office of Administrative Law (OAL) only			
NOTICE		REGULATIONS	
AGENCY WITH RULEMAKING AUTHORITY State Board of Equalization			AGENCY FILE NUMBER (if any)

2014 MAY -9 AM 11:11  
OFFICE OF ADMINISTRATIVE LAW

ENDORSED FILED  
2014 JUN 11 PM 2:59  
Debra Bowen  
DEBRA BOWEN  
SECRETARY OF STATE

**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	ACTION ON PROPOSED NOTICE <input type="checkbox"/> Approved as Submitted <input type="checkbox"/> Approved as Modified <input type="checkbox"/> Disapproved/Withdrawn		NOTICE REGISTER NUMBER <b>2014, 72</b>	PUBLICATION DATE <b>2/14/2014</b>	

**B. SUBMISSION OF REGULATIONS (Complete when submitting regulations)**

1a. SUBJECT OF REGULATION(S) Returns, Defects and Replacements		1b. ALL PREVIOUS RELATED OAL REGULATORY ACTION NUMBER(S)	
2. SPECIFY CALIFORNIA CODE OF REGULATIONS TITLE(S) AND SECTION(S) (Including title 26, if toxics related)			
SECTION(S) AFFECTED (List all section number(s) individually. Attach additional sheet if needed.)		ADOPT	
		AMEND	
18		1655	
TITLE(S)		REPEAL	
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 January 1, April 1, July 1, or October 1 (Gov. Code §11343.4(a))	<input type="checkbox"/> Effective on filing with Secretary of State	<input type="checkbox"/> §100 Changes Without Regulatory Effect	<input type="checkbox"/> Effective other (Specify)
6. CHECK IF THESE REGULATIONS REQUIRE NOTICE TO, OR REVIEW, CONSULTATION, APPROVAL OR CONCURRENCE BY, ANOTHER AGENCY OR ENTITY			
<input type="checkbox"/> Department of Finance (Form STD. 399) (SAM §6660)	<input type="checkbox"/> Fair Political Practices Commission	<input type="checkbox"/> State Fire Marshal	
<input type="checkbox"/> Other (Specify) _____			
7. CONTACT PERSON Rick Bennion	TELEPHONE NUMBER (916) 445-2130	FAX NUMBER (Optional) (916) 324-3984	E-MAIL ADDRESS (Optional) rbennion@boe.ca.gov

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

SIGNATURE OF AGENCY HEAD OR DESIGNEE <i>Joann Richmond</i>	DATE May 6, 2014
TYPED NAME AND TITLE OF SIGNATORY Joann Richmond, Chief, Board Proceedings Division	

For use by Office of Administrative Law (OAL) only

ENDORSED APPROVED

JUN 11 2014

Office of Administrative Law

**Final Text of Proposed Amendments to  
California Code of Regulations, Title 18, Section 1655**

**1655. Returns, Defects and Replacements.**

(a) Returned Merchandise.

(1) In General. Except as provided in paragraph (2) of this subdivision, the amount upon which tax is computed does not include the amount charged for merchandise returned by customers if, (1) the full sale price, including that portion designated as "sales tax," is refunded either in cash or credit, and (2) the customer, in order to obtain the refund or credit, is not required to purchase other property at a price greater than the amount charged for the property that is returned. Refund or credit of the entire amount is deemed to be given when the purchase price, less rehandling and restocking costs, is refunded or credited to the customer. The amount withheld for rehandling and restocking may not exceed the actual cost of rehandling and restocking the returned merchandise. However, in lieu of using the actual cost for each transaction, the amount withheld for rehandling and restocking may be a percentage of the sales price determined by the average cost of rehandling and restocking returned merchandise during the previous accounting cycle (generally one year). If the seller elects to withhold rehandling and restocking amounts based on a percentage of sales price, the seller is bound by that election for the entire accounting cycle for which the election is made and must apply that percentage in lieu of actual cost during that period on all returned merchandise transactions for which rehandling and restocking costs are withheld. The amount withheld as rehandling and restocking costs may not include compensation for increased overhead costs because of the return, for refinishing or restoring the property to salable condition where the necessity therefore is occasioned by customer usage, or for any expense prior to the "sale" (i.e., transfer of title, lease, or possession under a conditional sale contract). Sellers must maintain adequate records which may be verified by audit, documenting the percentage used.

(2) Contract Cancellation Options Required by Car Buyer's Bill of Rights.

(A) Contract Cancellation Option. On and after July 1, 2006, the terms "gross receipts" and "sales price" do not include the purchase price for a contract cancellation option agreement with respect to a contract to purchase a used vehicle with a purchase price of less than forty thousand dollars (\$40,000), which a dealer is required to offer to a buyer pursuant to Vehicle Code section 11713.21. The purchase price for a contract cancellation option described in this subparagraph shall not exceed:

1. Seventy-five dollars (\$75) for a vehicle with a cash price of five thousand dollars (\$5,000) or less;
2. One hundred fifty dollars (\$150) for a vehicle with a cash price of more than five thousand dollars (\$5,000), but not more than ten thousand dollars (\$10,000);
3. Two hundred fifty dollars (\$250) for a vehicle with a cash price of more than ten thousand dollars (\$10,000), but not more than thirty thousand dollars (\$30,000); or

4. One percent of the purchase price for a vehicle with a cash price of more than thirty thousand dollars (\$30,000), but less than forty thousand dollars (\$40,000).

(B) Restocking Fee. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include the dollar amount of a restocking fee the buyer must pay to the dealer to exercise the right to cancel a purchase of a used car under a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph. The dollar amount of a restocking fee described in this subparagraph shall not exceed:

1. One hundred seventy-five dollars (\$175) if the vehicle’s cash price is five thousand dollars (\$5,000) or less;
2. Three hundred fifty dollars (\$350) if the vehicle’s cash price is more than five thousand dollars (\$5,000), but less than ten thousand dollars (\$10,000); or
3. Five hundred dollars (\$500) if the vehicle’s cash price is ten thousand dollars (\$10,000) or more.

(C) Amounts Refunded to Customers. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include that portion of the selling price for a used motor vehicle that is refunded to the buyer due to the buyer’s exercise of the right to return the vehicle for a refund, which is contained in a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph.

(b) Defective Merchandise.

(1) In General. Amounts credited or refunded by sellers to consumers on account of defects in merchandise sold may be excluded from the amount on which tax is computed. If, however, defective merchandise is accepted as part payment for other merchandise and an additional allowance or credit is given on account of its defective condition, only the amount allowed or credited on account of defects may be excluded from taxable gross receipts. The amount allowed as the “trade-in” value must be included in the measure of tax.

(2) Restitution or Replacement Under California Lemon Law.

(A) General. Under subdivision (d) of Civil Code section 1793.2, if a manufacturer is unable to service or repair a “new motor vehicle,” as that term is defined in subdivision (e)(2) of Civil Code section 1793.22, to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer must either replace the motor vehicle or provide the buyer restitution of the purchase price, less specified amounts, at the buyer’s election.

For purposes of this regulation, the term buyer shall include a lessee of a new motor vehicle.

(B) Restitution. A manufacturer who pays a buyer restitution pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 is entitled to a refund of the amount of sales or use tax, or sales tax reimbursement included in the restitution paid by the manufacturer to the buyer. The manufacturer may file a claim for refund of that amount with the Bboard. The claim must include a statement that the claim is submitted in accordance with the provisions of section 1793.25 of the Civil Code. The manufacturer must submit with the claim documents evidencing that restitution was made pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 including: a copy of the original sales or lease agreement between the buyer and the dealer or lessor of the non-conforming motor vehicle; copies of documents showing all deductions made in calculating the amount of restitution paid to the buyer along with full explanations for those deductions, including settlement documents and odometer statements; a copy of the title branded “Lemon Law Buyback” for the non-conforming motor vehicle returned by the buyer; and proof that the decal the manufacturer is required to affix to that motor vehicle has been so affixed in accordance with section 11713.12 of the Vehicle Code. The manufacturer must also submit with the claim the seller’s permit number of the dealer or lessor who made the retail sale or lease of the non-conforming motor vehicle to the buyer, and evidence for one of the following:

1. that ~~that~~ The dealer had reported and paid sales tax on the gross receipts from that sale; or

2. The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state; or

3. The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer restitution is not relevant for purposes of determining whether restitution has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(C) Replacement. For purposes of this regulation, a manufacturer who, pursuant to subdivision (d)(2) of Civil Code section 1793.2, replaces a non-conforming motor vehicle with a new motor vehicle substantially identical to the motor vehicle replaced is replacing the motor vehicle under the terms of the mandatory warranty. No additional tax is due unless the buyer is required to pay an additional amount to receive the replacement motor vehicle, in which case tax is due measured by the amount of that payment. If an amount is refunded to the customer as part of the exchange of the non-conforming motor vehicle for the replacement motor vehicle, then that amount is regarded as restitution for purposes of this regulation if it satisfies the requirements of subdivision (d)(2) of Civil Code section 1793.2. The manufacturer may file a claim for refund under subdivision (b)(2)(B) of this regulation for the amount of sales or use tax, or sales tax reimbursement that is included in the amount of that restitution paid by the manufacturer to the buyer.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer a replacement is not relevant for purposes of determining whether the replacement has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(D) The amount of use tax the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee pursuant to Civil Code section 1793.2.

(c) Replacement Parts -Warranties.

(1) In General -Definitions. “Mandatory Warranty.” A warranty is mandatory within the meaning of this regulation when the buyer, as a condition of the sale, is required to purchase the warranty or guaranty contract from the seller. “Optional Warranty.” A warranty is optional within the meaning of this regulation when the buyer is not required to purchase the warranty or guaranty contract from the seller, i.e., the buyer is free to contract with anyone he or she chooses.

(2) Mandatory Warranties. The sale of tangible personal property includes the furnishing, pursuant to the guaranty provisions of the contract of sale, or mandatory warranty, of replacement parts or materials, and if the property subject to the warranty is sold at retail, the measure of the tax includes any amount charged for the guaranty or warranty, whether or not separately stated. The sale of the replacement parts and materials to the seller furnishing them thereunder is a sale for resale and not taxable.

(3) Optional Warranties. The person obligated under an optional warranty contract to furnish parts, materials, and labor necessary to maintain the property is the consumer of the materials and parts furnished and tax applies to the sale of such items to that person. If he or she purchased the property for resale or from outside California, without tax paid on the purchase price, he or she must report and pay tax upon the cost of such property to him or her when he or she appropriates it to the fulfillment of the contract of warranty.

(4) Deductibles. A deductible paid by a customer under the terms of a mandatory or optional warranty contract is subject to tax measured by the amount of the deductible allocable to the sale of tangible personal property to the customer. For example, if the itemized sales price of tangible personal property (or the fair retail value if not separately itemized) provided pursuant to a warranty is 50 percent of the total fair retail value of the repairs and the deductible is \$100, 50 percent of that deductible, \$50, would be allocable to the sale of tangible personal property and would be subject to tax, whether the warranty were optional or mandatory. Unless otherwise stated in the warranty contract, when either an optional or a mandatory warranty provides that the customer will pay a deductible towards repairs and services provided under the warranty, the person providing the warranty contract is liable for any tax or tax reimbursement otherwise payable by the customer with respect to that deductible.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6006-6012 and 6012.3, Revenue and Taxation Code; Sections 1793.2-1793.25, Civil Code; and Sections 11713.12 and 11713.21, Vehicle Code.

**SUMMARY OF REGULATORY  
ACTIONS**

**REGULATIONS FILED WITH  
SECRETARY OF STATE**

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

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

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

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

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

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

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

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

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

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

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

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

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Title 18. Public Revenue  
Sales and Use Tax

Regulation 1655, *Returns, Defects and Replacements*

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  - Email sent to Interested Parties, February 14, 2014
  - CA Regulatory Notice Register 2014, Volume No. 7-Z
8. [Notice to Interested Parties, February 14, 2014](#)

The following items are exhibited:

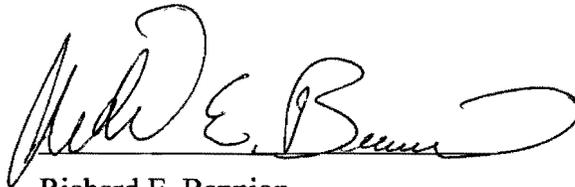
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  - Notice of Proposed Regulatory Action
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## VERIFICATION

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 May 6, 2014 . The file was reopened on June 10, 2014 for changes requested by OAL with the Final Statement of Reasons and the file was closed on June 11, 2014, 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.

June 11, 2014

A handwritten signature in black ink, appearing to read "Richard E. Bennion", written over a horizontal line.

Richard E. Bennion  
Regulations Coordinator  
State Board of Equalization

**Final Statement of Reasons for the Adoption of the  
Proposed Amendments to California Code of Regulations,  
Title 18, Section 1655, *Returns, Defects and Replacements***

Update of Information in the Initial Statement of Reasons

The State Board of Equalization (Board) held a public hearing regarding the proposed amendments to California Code of Regulations, title 18, section (Regulation) 1655, *Returns, Defects and Replacements*, on April 22, 2014. During the public hearing, the Board unanimously voted to adopt the proposed amendments to Regulation 1655 without making any changes. The Board did not receive any written comments regarding the proposed regulatory action and no interested parties appeared at the public hearing on April 22, 2014, to comment on the proposed regulatory action.

The factual basis, specific purpose, and necessity for, the problem to be addressed by, and the anticipated benefit from the adoption of the proposed amendments to Regulation 1655 are the same as provided in the initial statement of reasons. The Board anticipates that the proposed amendments will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25 (of “the Lemon Law”) by Assembly Bill No. 242 (AB 242) (Stats. 2011, ch. 727, §§ 1 and 2) by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242);
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively;
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242); and
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).

The adoption of the proposed amendments to Regulation 1655 is not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to Regulation 1655 or the proposed amendments to Regulation 1655.

The Board did not rely on any data or any technical, theoretical, or empirical study, report, or similar document in proposing or adopting the proposed amendments to Regulation 1655 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, the Board’s determination that the proposed regulatory action is not a major regulation, as defined in

Government Code section 1134.548 and California Code of Regulations, title 1, section 2000, and the Board's economic impact assessment, 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 benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

The proposed amendments to Regulation 1655 may affect small business.

Furthermore, the proposed amendments to Regulation 1655, subdivision (b)(2), duplicate some of the provisions in Civil Code section 1793.25, which is cited in the regulation's "reference" note, and the duplication is necessary to satisfy the "clarity" standard of Government Code section 11349.1, subdivision (a)(3), by providing those subject to the regulation with all the relevant statutory requirements in one place.

#### No Mandate on Local Agencies or School Districts

The Board has determined that the adoption of the proposed amendments to Regulation 1655 does not impose a mandate on local agencies or school districts.

#### Public Comments

The Board did not receive any written comments regarding the proposed regulatory action and no interested parties appeared at the public hearing on April 22, 2014, to comment on the proposed regulatory action.

#### Determinations Regarding Alternatives

By its motion on April 22, 2014, the Board determined that no alternative to the proposed amendments to Regulation 1655 would be more effective in carrying out the purposes for which the amendments are proposed, would be as effective and less burdensome to affected private persons than the adopted amendments, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or provisions of law.

The Board did not reject any reasonable alternative to the proposed amendments to Regulation 1655 that would lessen any adverse impact the proposed action may have on small business.

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.

**Updated Informative Digest for the State Board of Equalization’s  
Adoption of Proposed Amendments to California Code of Regulations,  
Title 18, Section 1655, *Returns, Defects and Replacements***

The State Board of Equalization (Board) held a public hearing regarding the proposed amendments to California Code of Regulations, title 18, section (Regulation) 1655, *Returns, Defects and Replacements*, on April 22, 2014. During the public hearing, the Board unanimously voted to adopt the proposed amendments to Regulation 1655 without making any changes.

The Board did not receive any written comments regarding the proposed regulatory action and no interested parties appeared at the public hearing on April 22, 2014, to comment on the proposed regulatory action. There have not been any changes to the applicable laws or the effect of, the objective of, and anticipated benefits from the adoption of the proposed amendments to Regulation 1655 described in the informative digest included in the notice of proposed regulatory action. The informative digest included in the notice of proposed regulatory action provides:

Current Law

*General*

The Song-Beverly Consumer Warranty Act (commencing with Civ. Code, § 1790) contains provisions that provide warranty protections to purchasers of both new and used consumer goods. The act includes provisions (Civ. Code §§ 1793.2 - 1793.26) that require compensation to California consumers of defective new motor vehicles – provisions commonly referred to as California’s “Lemon Law.” The Lemon Law provides, in relevant part, that if a manufacturer or its representative in this state, such as an authorized dealer, is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer is required to either promptly replace the vehicle or make restitution to the buyer. (Civ. Code, § 1793.2, subd. (d)(2).)

Under the existing Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.), a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant here, a “sale” and a “purchase.” (Rev. & Tax. Code, §§ 6006, 6010.) For a lease that is a “sale” and a “purchase,” the tax is measured by the rentals payable. However, as provided in subdivision (c)(1) of Regulation 1660, *Leases of Tangible Personal Property – In General*, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686, *Receipts for Tax Paid to Retailers*. The

lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

The Lemon Law originally provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other collateral charges, *sales* tax. (Civ. Code, § 1793.2.) The Lemon Law further required the Board to reimburse the manufacturer for an amount equal to the *sales* tax which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer when satisfactory proof was provided that the retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale, and that the manufacturer had complied with the requirements of Civil Code section 1793.23, subdivision (c). However, the Lemon Law was silent with respect to whether restitution was required to include *use* tax and whether the Board was required to reimburse a manufacturer for use tax paid to or for a buyer or lessee or included in restitution paid to a buyer or lessee.

As relevant here, AB 242 amended the Lemon Law, specifically Civil Code sections 1793.2 and 1793.25, to make technical corrections sponsored by the Board. The amendments clarify that restitution, under the Lemon Law, includes *use* tax paid or payable by a buyer, including a lessee, of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to the Lemon Law. And, AB 242 provides that the Board-sponsored amendments to the Lemon Law are declaratory of existing law. (AB 242, § 21.)

In the case of restitution, Civil Code section 1793.2, subdivision (d)(2)(B) now provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer, including any collateral charges “such as sales or use tax.” And, Civil Code section 1793.2, subdivision (d)(2)(D) now specifies that “Pursuant to Section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

With respect to reimbursement, Civil Code section 1793.25, subdivision (a) now expressly requires the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to “the sales tax or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or includes in making restitution to the buyer “or lessee” under the Lemon Law, and, as a condition to receiving reimbursement, requires a manufacturer to provide satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of that motor vehicle.

Also, Civil Code section 1793.25, subdivision (e) now provides that “The amount of use tax that the State Board of Equalization is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee” under the Lemon Law.

Effect, Objective, and Benefits of the Proposed Amendments to Regulation 1655

*Need for Clarification*

Subdivision (b)(2) of Regulation 1655 explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. However, Regulation 1655 does not indicate that AB 242 clarified that, under the Lemon Law, restitution includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle and required the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or includes in making restitution to a buyer or lessee, under the Lemon Law. Therefore, the Board’s Business Taxes Committee (BTC) staff determined that amendments to Regulation 1655 are needed in order to make the regulation consistent with and implement, interpret, and make specific AB 242’s amendments to the Lemon Law set forth above.

*Interested Parties Process*

As a result of AB 242, BTC staff drafted amendments to Regulation 1655. Specifically, the draft amendments suggested adding language to Regulation 1655, subdivision (b)(2)(A) to incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D), by specifying that, for purposes of Regulation 1655, the term buyer includes a lessee of a new motor vehicle. The draft amendments suggested adding “or use” tax to where the current regulation refers to “sales tax or sales tax

reimbursement” in subdivision (b)(2)(B) and (C). The draft amendments suggested adding “or lease” after “sales” where the current regulation refers to “sales agreement” and after “sale” where the current regulation refers to “retail sale” in subdivision (b)(2)(B). The draft amendments also suggested adding “or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer” in subdivision (b)(2)(B).

In addition, the draft amendments suggested revising and reformatting the last sentence in Regulation 1655, subdivision (b)(2)(B), which currently requires a manufacturer, when filing a claim for refund for sales tax or sales tax reimbursement included in restitution paid to a buyer, to submit evidence that the dealer who made the retail sale of the non-conforming vehicle to that buyer reported and paid sales tax on the gross receipts from that sale. The revised and reformatted sentence requires a manufacturer, when filing a claim for refund for sales or use tax or sales tax reimbursement included in restitution paid to a buyer, including a lessee, under the Lemon Law, to provide “evidence of one of the following” from a list that includes proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The draft amendments also suggested adding a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

BTC staff subsequently prepared a discussion paper regarding the amendments made to the Lemon Law by AB 242 and staff’s draft amendments to Regulation 1655, provided the discussion paper and its draft amendments to Regulation 1655 to the interested parties, and conducted an interested parties meeting on August 8, 2013, to discuss the draft amendments to Regulation 1655. During the interested parties meeting, a participant inquired as to how the provisions of Regulation 1655 would apply to a transaction in which a lessor paid tax at the time the lessor purchased a vehicle which the lessor would then lease. Staff considered the scenario and, subsequent to the meeting, staff explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement from the lessor. (See Reg. 1660, subd. (c)(2) and (3), regarding property purchased tax-paid and leased in substantially the same form as acquired.) And, staff explained that, with respect to sales tax transactions, the existing provisions of

Regulation 1655 would apply to a manufacturer's claim for a refund for sales tax reimbursement the manufacturer included in restitution paid to a lessor, under the Lemon Law. Furthermore, staff noted that AB 242 did not change the application of the Lemon Law to sales tax transactions, and that questions regarding the application of Regulation 1655 to sales tax transactions were beyond the scope of the current interested parties process, which was to discuss the issue of whether to amend Regulation 1655 to clarify the new provisions of the Lemon Law applicable to use tax transactions.

Since BTC staff did not receive any other inquiries or comments regarding its draft amendments during or subsequent to the first interested parties meeting and staff had no changes to its recommendation to amend Regulation 1655, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff's draft amendments. Staff also notified interested parties that comments could be submitted up to October 17, 2013, for consideration in the preparation of a Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

*December 17, 2013, BTC Meeting*

Subsequently, staff prepared Formal Issue Paper 13-012 and distributed it to the Board Members for consideration at the Board's December 17, 2013, BTC meeting. Formal Issue Paper 13-012 recommended that the Board approve and authorize publication of the amendments to Regulation 1655 (discussed above) in order to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).

During the December 17, 2013, BTC meeting, the Board Members unanimously voted to propose the amendments to Regulation 1655 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1655 are reasonably necessary to have the effect and accomplish the objective of making the regulation consistent with and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1655 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 1655 is the only state regulation prescribing the requirements for the Board to reimburse a manufacturer under Civil Code section 1793.25. In addition, the Board has determined that there are no comparable federal regulations or statutes to Regulation 1655 or the proposed amendments to Regulation 1655.



## BOARD OF EQUALIZATION

**BUSINESS TAXES COMMITTEE MEETING MINUTES**

HONORABLE BETTY T. YEE, COMMITTEE CHAIR

450 N STREET, SACRAMENTO

MEETING DATE: DECEMBER 17, 2013, TIME: 10:00 A.M.

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**ACTION ITEMS & STATUS REPORT ITEMS****Agenda Item No: 1****Title: Proposed Amendments to Regulation 1655, *Returns, Defects and Replacements*.****Issue:**

Whether the Board should amend Sales and Use Tax Regulation (Regulation) 1655, *Returns, Defects and Replacements*, in order to implement, interpret, and make specific the amendments made to Civil Code sections 1793.2 and 1793.25, by Assembly Bill 242 (AB 242)(Stat. 2011, Ch. 727).

**Committee Discussion:**

Staff introduced the issue. There was no discussion of this item.

**Committee Action:**

Upon motion by Mr. Runner and seconded by Mr. Horton, without objection, the Committee approved and authorized for publication the proposed amendments to Regulation 1655, *Returns, Defects and Replacements*. A copy of the proposed amendments to Regulation 1655 is attached.

**Agenda Item No: 2****Title: Proposed Amendments to Regulation 4902, *Relief From Liability*, for the extension of relief based on written advice.****Issue:**

Should the Board revise Regulation 4902, *Relief From Liability*, to extend relief of liability for reliance upon written advice or reliance on a prior audit to another person if that person has a common controlling ownership, and shares accounting functions with the written advice recipient?

**Committee Discussion:**

Staff introduced the issue and explained that the proposed amendments would extend relief of liability under specific circumstances. Staff also explained that a revision to the proposed amendments was recommended subsequent to the distribution of the issue paper and related materials. Staff requested that the proposed amendments include changing the term "that person" to "those persons" at the end of the second paragraph in subdivision (a).

Staff further noted that the proposed amendments, inclusive of the additional revision, conform Regulation 4902 with the revisions to Sales and Use Tax Regulation 1705, *Relief From Liability*, approved at the August 13, 2013 Business Taxes Committee meeting.

**Committee Action:**

Upon motion by Mr. Horton and seconded by Ms. Steel, without objection, the Committee approved and authorized for publication the proposed amendments to Regulation 4902, *Relief From Liability*, inclusive of changing the term “that person” to “those persons” at the end of the second paragraph in subdivision (a). A copy of the proposed amendments to Regulation 4902 is attached.

/s/ Betty T. Yee

Honorable Betty T. Yee, Committee Chair

/s/ Cynthia Bridges

Cynthia Bridges, Executive Director

BOARD APPROVED

at the December 17, 2013 Board Meeting

/s/ Joann Richmond

Joann Richmond, Chief  
Board Proceedings Division

**Regulation 1655, Returns, Defects and Replacements**

Reference: Sections 6006-6012 and 6012.3, Revenue and Taxation Code; Sections 1793.2-1793.25, Civil Code; and Sections 11713.12 and 11713.21, Vehicle Code.

**(a) Returned Merchandise.**

(1) In General. Except as provided in paragraph (2) of this subdivision, the amount upon which tax is computed does not include the amount charged for merchandise returned by customers if, (1) the full sale price, including that portion designated as "sales tax," is refunded either in cash or credit, and (2) the customer, in order to obtain the refund or credit, is not required to purchase other property at a price greater than the amount charged for the property that is returned. Refund or credit of the entire amount is deemed to be given when the purchase price, less rehandling and restocking costs, is refunded or credited to the customer. The amount withheld for rehandling and restocking may not exceed the actual cost of rehandling and restocking the returned merchandise. However, in lieu of using the actual cost for each transaction, the amount withheld for rehandling and restocking may be a percentage of the sales price determined by the average cost of rehandling and restocking returned merchandise during the previous accounting cycle (generally one year). If the seller elects to withhold rehandling and restocking amounts based on a percentage of sales price, the seller is bound by that election for the entire accounting cycle for which the election is made and must apply that percentage in lieu of actual cost during that period on all returned merchandise transactions for which rehandling and restocking costs are withheld. The amount withheld as rehandling and restocking costs may not include compensation for increased overhead costs because of the return, for refinishing or restoring the property to salable condition where the necessity therefore is occasioned by customer usage, or for any expense prior to the "sale" (i.e., transfer of title, lease, or possession under a conditional sale contract). Sellers must maintain adequate records which may be verified by audit, documenting the percentage used.

**(2) Contract Cancellation Options Required by Car Buyer's Bill of Rights.**

(A) Contract Cancellation Option. On and after July 1, 2006, the terms "gross receipts" and "sales price" do not include the purchase price for a contract cancellation option agreement with respect to a contract to purchase a used vehicle with a purchase price of less than forty thousand dollars (\$40,000), which a dealer is required to offer to a buyer pursuant to Vehicle Code section 11713.21. The purchase price for a contract cancellation option described in this subparagraph shall not exceed:

1. Seventy-five dollars (\$75) for a vehicle with a cash price of five thousand dollars (\$5,000) or less;
2. One hundred fifty dollars (\$150) for a vehicle with a cash price of more than five thousand dollars (\$5,000), but not more than ten thousand dollars (\$10,000);

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The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

3. Two hundred fifty dollars (\$250) for a vehicle with a cash price of more than ten thousand dollars (\$10,000), but not more than thirty thousand dollars (\$30,000); or
4. One percent of the purchase price for a vehicle with a cash price of more than thirty thousand dollars (\$30,000), but less than forty thousand dollars (\$40,000).

(B) Restocking Fee. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include the dollar amount of a restocking fee the buyer must pay to the dealer to exercise the right to cancel a purchase of a used car under a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph. The dollar amount of a restocking fee described in this subparagraph shall not exceed:

1. One hundred seventy-five dollars (\$175) if the vehicle's cash price is five thousand dollars (\$5,000) or less;
2. Three hundred fifty dollars (\$350) if the vehicle's cash price is more than five thousand dollars (\$5,000), but less than ten thousand dollars (\$10,000); or
3. Five hundred dollars (\$500) if the vehicle's cash price is ten thousand dollars (\$10,000) or more.

(C) Amounts Refunded to Customers. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include that portion of the selling price for a used motor vehicle that is refunded to the buyer due to the buyer's exercise of the right to return the vehicle for a refund, which is contained in a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph.

(b) Defective Merchandise.

(1) In General. Amounts credited or refunded by sellers to consumers on account of defects in merchandise sold may be excluded from the amount on which tax is computed. If, however, defective merchandise is accepted as part payment for other merchandise and an additional allowance or credit is given on account of its defective condition, only the amount allowed or credited on account of defects may be excluded from taxable gross receipts. The amount allowed as the “trade-in” value must be included in the measure of tax.

(2) Restitution or Replacement Under California Lemon Law.

(A) General. Under subdivision (d) of Civil Code section 1793.2, if a manufacturer is unable to service or repair a “new motor vehicle,” as that term is defined in subdivision (e)(2) of Civil Code section 1793.22, to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer must either replace the motor vehicle or provide the buyer restitution of the purchase price, less specified amounts, at the buyer's election.

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The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

For purposes of this regulation, the term buyer shall include a lessee of a new motor vehicle.

(B) Restitution. A manufacturer who pays a buyer restitution pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 is entitled to a refund of the amount of sales or use tax, or sales tax reimbursement included in the restitution paid by the manufacturer to the buyer. The manufacturer may file a claim for refund of that amount with the Board. The claim must include a statement that the claim is submitted in accordance with the provisions of section 1793.25 of the Civil Code. The manufacturer must submit with the claim documents evidencing that restitution was made pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 including: a copy of the original sales or lease agreement between the buyer and the dealer or lessor of the non-conforming motor vehicle; copies of documents showing all deductions made in calculating the amount of restitution paid to the buyer along with full explanations for those deductions, including settlement documents and odometer statements; a copy of the title branded "Lemon Law Buyback" for the non-conforming motor vehicle returned by the buyer; and proof that the decal the manufacturer is required to affix to that motor vehicle has been so affixed in accordance with section 11713.12 of the Vehicle Code. The manufacturer must also submit with the claim the seller's permit number of the dealer or lessor who made the retail sale or lease of the non-conforming motor vehicle to the buyer, and evidence for one of the following:

1. that ~~the~~ the dealer had reported and paid sales tax on the gross receipts from that sale; or
2. The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state; or
3. The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer restitution is not relevant for purposes of determining whether restitution has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(C) Replacement. For purposes of this regulation, a manufacturer who, pursuant to subdivision (d)(2) of Civil Code section 1793.2, replaces a non-conforming motor vehicle with a new motor vehicle substantially identical to the motor vehicle replaced is replacing the motor vehicle under the terms of the mandatory warranty. No additional tax is due unless the buyer is required to pay an additional amount to receive the replacement motor vehicle, in which case tax is due measured by the amount of that payment. If an amount is refunded to the customer as part of the exchange of the non-conforming motor vehicle for the replacement motor vehicle, then that amount is regarded as restitution for purposes of this regulation if it satisfies the requirements of subdivision (d)(2) of Civil Code section 1793.2. The manufacturer may file a claim for refund under subdivision

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The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

(b)(2)(B) of this regulation for the amount of sales or use tax, or sales tax reimbursement that is included in the amount of that restitution paid by the manufacturer to the buyer. For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer a replacement is not relevant for purposes of determining whether the replacement has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(D) The amount of use tax the board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee pursuant to Civil Code section 1793.2.

(c) Replacement Parts -Warranties.

(1) In General -Definitions. "Mandatory Warranty." A warranty is mandatory within the meaning of this regulation when the buyer, as a condition of the sale, is required to purchase the warranty or guaranty contract from the seller. "Optional Warranty." A warranty is optional within the meaning of this regulation when the buyer is not required to purchase the warranty or guaranty contract from the seller, i.e., the buyer is free to contract with anyone he or she chooses.

(2) Mandatory Warranties. The sale of tangible personal property includes the furnishing, pursuant to the guaranty provisions of the contract of sale, or mandatory warranty, of replacement parts or materials, and if the property subject to the warranty is sold at retail, the measure of the tax includes any amount charged for the guaranty or warranty, whether or not separately stated. The sale of the replacement parts and materials to the seller furnishing them thereunder is a sale for resale and not taxable.

(3) Optional Warranties. The person obligated under an optional warranty contract to furnish parts, materials, and labor necessary to maintain the property is the consumer of the materials and parts furnished and tax applies to the sale of such items to that person. If he or she purchased the property for resale or from outside California, without tax paid on the purchase price, he or she must report and pay tax upon the cost of such property to him or her when he or she appropriates it to the fulfillment of the contract of warranty.

(4) Deductibles. A deductible paid by a customer under the terms of a mandatory or optional warranty contract is subject to tax measured by the amount of the deductible allocable to the sale of tangible personal property to the customer. For example, if the itemized sales price of tangible personal property (or the fair retail value if not separately itemized) provided pursuant to a warranty is 50 percent of the total fair retail value of the repairs and the deductible is \$100, 50 percent of that deductible, \$50, would be allocable to the sale of tangible personal property and would be subject to tax, whether the warranty were optional or mandatory. Unless otherwise stated in the warranty contract, when either an optional or a mandatory warranty provides that the customer will pay a deductible towards repairs and services provided under the warranty, the person providing the warranty contract is liable for any tax or tax reimbursement otherwise payable by the customer with respect to that deductible.

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The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

**REGULATION 4902, RELIEF FROM LIABILITY**

*Reference:* Sections 7657.1, 8879, 30284, 32257, 40104, 41098, 43159, 45157, 46158, 50112.5, 55045, and 60210, Revenue and Taxation Code.

**(a) GENERAL.** A person may be relieved from the liability for the payment of tax, defined in section 4901(a)(7), imposed pursuant to applicable tax laws, defined in section 4901(a)(1), including any penalties and interest added to the tax, when that liability resulted from the failure to make a timely return or a payment and such failure was found by the board to be due to reasonable reliance on:

(1) Written advice given by the board under the conditions set forth in subdivision (b) below, or

(2) Written advice in the form of an annotation or legal ruling of counsel under the conditions set forth in subdivision (d) below; or

(3) Written advice given by the board in a prior audit ~~of that person~~ under the conditions set forth in subdivision (c) below. As used in this regulation, the term "prior audit" means any audit conducted prior to the current examination where the issue in question was examined.

Written advice from the board may only be relied upon by the person to whom it was originally issued or a legal or statutory successor to that person. Written advice from the board which was received during a prior audit of the person under the conditions set forth in subdivision (c) below, may be relied upon by the person audited or a person with shared accounting and common ownership with the audited person or by a legal or statutory successor to ~~that~~those persons.

The term "written advice" includes advice that was incorrect at the time it was issued as well as advice that was correct at the time it was issued, but, subsequent to issuance, was invalidated by a change in statutory or constitutional law, by a change in board regulations, or by a final decision of a court of competent jurisdiction. Prior written advice may not be relied upon subsequent to: (1) the effective date of a change in statutory or constitutional law and board regulations or the date of a final decision of a court of competent jurisdiction regardless that the board did not provide notice of such action; or (2) the person receiving a subsequent writing notifying the person that the advice was not valid at the time it was issued or was subsequently rendered invalid. As generally used in this regulation, the term "written advice" includes both written advice provided in a written communication under

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The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

subdivision (b) below and written advice provided in a prior audit of the person under subdivision (c) below.

**(b) ADVICE PROVIDED IN A WRITTEN COMMUNICATION.** Advice from the board provided to the person in a written communication must have been in response to a specific written inquiry from the person seeking relief from liability, or from his or her representative. To be considered a specific written inquiry for purposes of this regulation, representatives must identify the specific person for whom the advice is requested. Such inquiry must have set forth and fully described the facts and circumstances of the activity or transactions for which the advice was requested.

**(c) WRITTEN ADVICE PROVIDED IN A PRIOR AUDIT.** Presentation of the person's books and records for examination by an auditor shall be deemed to be a written request for the audit report by the audited person and any person with shared accounting and common ownership with the audited person. If a prior audit report of the person requesting relief contains written evidence which demonstrates that the issue in question was examined, either in a sample or census (actual) review, such evidence will be considered "written advice from the board" for purposes of this regulation. A census, (actual) review, as opposed to a sample review, involves examination of 100% of the person's transactions pertaining to the issue in question. For written advice contained in a prior audit of the person to apply to the person's activity or transaction in question, the facts and conditions relating to the activity or transaction must not have changed from those which occurred during the period of operation in the prior audit. Audit comments, schedules, and other writings prepared by the board that become part of the audit work papers which reflect that the activity or transaction in question was properly reported and no amount was due are sufficient for a finding for relief from liability, unless it can be shown that the person seeking relief knew such advice was erroneous.

For the purposes of this section a person is considered to have shared accounting and common ownership if the person:

- (1) Is engaged in the same line of business as the audited person,
- (2) Has common verifiable controlling ownership of 50% or greater ownership or has a common majority shareholder with the audited person, and
- (3) Shares centralized accounting functions with the audited person. The audited person routinely follows the same business practices that are followed by each entity involved. Evidence that may indicate sharing of centralized accounting functions includes, but is not limited to, the following:

\*\*\*

The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

- A. Quantifiable control of the accounting practices of each business by the common ownership or management that dictates office policies for accounting and tax return preparation.
- B. Shared accounting staff or an outside firm who maintains books and records and prepares returns for tax and fee programs administered under the Revenue and Taxation Code sections referenced under this regulation.
- C. Shared accounting policies and procedures.

These requirements must be established as existing during the periods for which relief is sought. A subsequent written notification stating that the advice was not valid at the time it was issued or was subsequently rendered invalid to any party with shared accounting and common ownership, including the audited party, serves as notification to all parties with shared accounting and common ownership, including the audited party, that the prior written advice may not be relied upon as of the notification date.

**(d) ANNOTATIONS AND LEGAL RULINGS OF COUNSEL.** Advice from the board provided to the person in the form of an annotation or legal ruling of counsel shall constitute written advice only if:

(1) The underlying legal ruling of counsel involving the fact pattern at issue is addressed to the person or to his or her representative under the conditions set forth in subdivision (b) above.

(2) The annotation or legal ruling of counsel is provided to the person or his or her representative by the board within the body of a written communication and involves the same fact pattern as that presented in the subject annotation or legal ruling of counsel.

**(e) TRADE OR INDUSTRY ASSOCIATIONS.** A trade or industry association requesting advice on behalf of its member(s) must identify and include the specific member name(s) for whom the advice is requested for relief from liability under this regulation.

*History:* Adopted February 5, 2003, effective May 28, 2003. The underscored citation indicates an electronic hyperlink to the cite.

\*\*\*

The proposed amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

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MICHELLE STEEL  
Third District, Orange County

JEROME E. HORTON  
Fourth District, Los Angeles

JOHN CHIANG  
State Controller

CYNTHIA BRIDGES  
Executive Director

December 6, 2013

Dear Interested Party:

Enclosed are the Agenda, Issue Paper, and Revenue Estimate for the December 17, 2013 Business Taxes Committee meeting. This meeting will address the proposed amendments to Regulation 1655, *Returns, Defects and Replacements*, to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by Assembly Bill 242 (Stat. 2011, Ch. 727).

Please feel free to publish this information on your website or otherwise distribute it to your associates, members, or other persons that may be interested in this issue.

Thank you for your input on these issues and I look forward to seeing you at the Business Taxes Committee meeting at **10:00 a.m.** on **December 17, 2013** in Room 121 at the address shown above.

Sincerely,

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

SB:rsw

Enclosures

cc: (all with enclosures)

Honorable Jerome E. Horton, Chairman, Fourth District  
Honorable Michelle Steel, Vice Chair, Third District  
Honorable Betty T. Yee, Member, First District (MIC:71)  
Senator George Runner (Ret.), Member, Second District (via email)  
Honorable John Chiang, State Controller, c/o Ms. Marcy Jo Mandel

(via email)

Mr. David Hunter, Board Member's Office, Fourth District  
Mr. Michael Vigil, Board Member's Office, Fourth District  
Mr. Neil Shah, Board Member's Office, Third District  
Mr. Tim Treichelt, Board Member's Office, Third District  
Mr. Alan LoFaso, Board Member's Office, First District  
Ms. Mengjun He, Board Member's Office, First District  
Ms. Yvette Stowers, Board Member's Office, First District  
Mr. Ramon Salazar, Board Member's Office, First District  
Mr. Sean Wallentine, Board Member's Office, Second District  
Mr. James Kuhl, Board Member's Office, Second District  
Mr. Lee Williams, Board Member's Office, Second District  
Mr. Alan Giorgi, Board Member's Office, Second District  
Ms. Lynne Kinst, Board Member's Office, Second District  
Ms. Natasha Ralston Ratcliff, State Controller's Office  
Ms. Cynthia Bridges (MIC:73)  
Mr. Randy Ferris (MIC:83)  
Mr. Jeffrey L. McGuire (MIC:43)  
Mr. Robert Tucker (MIC:82)  
Mr. Bradley Heller (MIC:82)  
Mr. Lawrence Mendel (MIC:82)  
Ms. Monica Silva (MIC:82)  
Ms. Kirsten Stark (MIC:50)  
Mr. Clifford Oakes (MIC:50)  
Mr. Bradley Miller (MIC:92)  
Ms. Lynn Whitaker (MIC:50)  
Mr. Robert Wilke (MIC:50)



**AGENDA — December 17, 2013 Business Taxes Committee Meeting  
Proposed Amendments to Regulation 1655, Returns, Defects and Replacements**

**Action 1 – Staff  
Recommendation**

*(Only the proposed amendments to subdivision (b) of this regulation have been provided. Other subdivisions of the regulation are not being amended.)*

(b) Defective Merchandise.

(1) In General. Amounts credited or refunded by sellers to consumers on account of defects in merchandise sold may be excluded from the amount on which tax is computed. If, however, defective merchandise is accepted as part payment for other merchandise and an additional allowance or credit is given on account of its defective condition, only the amount allowed or credited on account of defects may be excluded from taxable gross receipts. The amount allowed as the “trade-in” value must be included in the measure of tax.

(2) Restitution or Replacement Under California Lemon Law.

(A) General. Under subdivision (d) of Civil Code section 1793.2, if a manufacturer is unable to service or repair a “new motor vehicle,” as that term is defined in subdivision (e)(2) of Civil Code section 1793.22, to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer must either replace the motor vehicle or provide the buyer restitution of the purchase price, less specified amounts, at the buyer's election.

For purposes of this regulation, the term buyer shall include a lessee of a new motor vehicle.

(B) Restitution. A manufacturer who pays a buyer restitution pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 is entitled to a refund of the amount of sales or use tax, or sales tax reimbursement included in the restitution paid by the manufacturer to the buyer. The manufacturer may file a claim for refund of that amount with the Board. The claim must include a statement that the claim is submitted in accordance with the provisions of section 1793.25 of the Civil Code. The manufacturer must submit with the claim documents evidencing that restitution was made pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 including: a copy of the original sales or lease agreement between the buyer and the dealer or lessor of the non-conforming motor vehicle; copies of documents showing all deductions made in calculating the amount of restitution paid to the buyer along with full explanations for those deductions, including settlement documents and odometer statements; a copy of the title branded “Lemon Law Buyback” for

**AGENDA — December 17, 2013 Business Taxes Committee Meeting**  
**Proposed Amendments to Regulation 1655, Returns, Defects and Replacements**

**Action 1 – Staff  
Recommendation**

the non-conforming motor vehicle returned by the buyer; and proof that the decal the manufacturer is required to affix to that motor vehicle has been so affixed in accordance with section 11713.12 of the Vehicle Code. The manufacturer must also submit with the claim the seller's permit number of the dealer or lessor who made the retail sale or lease of the non-conforming motor vehicle to the buyer, and evidence for one of the following:

1. that ~~the~~ The dealer had reported and paid sales tax on the gross receipts from that sale; or
2. The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state; or
3. The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer restitution is not relevant for purposes of determining whether restitution has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(C) Replacement. For purposes of this regulation, a manufacturer who, pursuant to subdivision (d)(2) of Civil Code section 1793.2, replaces a non-conforming motor vehicle with a new motor vehicle substantially identical to the motor vehicle replaced is replacing the motor vehicle under the terms of the mandatory warranty. No additional tax is due unless the buyer is required to pay an additional amount to receive the replacement motor vehicle, in which case tax is due measured by the amount of that payment. If an amount is refunded to the customer as part of the exchange of the non-conforming motor vehicle for the replacement motor vehicle, then that amount is regarded as restitution for purposes of this regulation if it satisfies the requirements of subdivision (d)(2) of Civil Code section 1793.2. The manufacturer may file a claim for refund under subdivision (b)(2)(B) of this regulation for the amount of sales or use tax, or sales tax reimbursement that is included in the amount of that restitution paid by the manufacturer to the buyer. For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer a replacement is not relevant for purposes of determining whether the replacement has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

**AGENDA — December 17, 2013 Business Taxes Committee Meeting**  
**Proposed Amendments to Regulation 1655, *Returns, Defects and Replacements***

<b>Action 1 – Staff Recommendation</b>	<u>(D) The amount of use tax the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee pursuant to Civil Code section 1793.2.</u>
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Issue Paper Number 13-012



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

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## Proposed Amendments to Regulation 1655, *Returns, Defects and Replacements*

### I. Issue

Whether the Board should amend Sales and Use Tax Regulation (Regulation) 1655, *Returns, Defects and Replacements*, in order to implement, interpret, and make specific the amendments made to Civil Code sections 1793.2 and 1793.25, by Assembly Bill 242 (AB 242)(Stat. 2011, Ch. 727). These sections require the Board of Equalization (BOE) to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California’s “Lemon Law.” Prior to AB 242, the Lemon Law only required reimbursement of sales tax or sales tax reimbursement.

### II. Alternative 1 – Staff Recommendation

Staff recommends the Board approve and authorize publication of the amendments to Regulation 1655, as set forth in Exhibit 2. Staff’s proposed amendments incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle.
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Expanding the list of evidence required of a manufacturer when filing a claim for refund.
- Specifying that the amount of use tax that BOE is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee.

For a more detailed explanation of Alternative 1 - Staff Recommendation, refer to section VI of this paper.

### III. Other Alternative Considered

Do not approve proposed amendments to Regulation 1655.

## IV. Background

### General

The Song-Beverly Consumer Warranty Act (commencing with Civil Code § 1790) contains provisions that provide warranty protections to purchasers of both new and used consumer goods. The act includes provisions (Civ. Code §§ 1793.2 through 1793.26) that require compensation to California consumers of defective new motor vehicles – provisions commonly referred to as California’s “Lemon Law.”

Under existing Sales and Use Tax Law, a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant to the issue in this paper, a “sale” and a “purchase” for purposes of that law. For a lease that is a “sale” and a “purchase,” the tax is measured by the rentals payable. However, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686. The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

### Prior to AB 242

Prior to AB 242, the Lemon Law provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other charges, *sales* tax, when satisfactory proof was provided that the retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale. These sections further required the BOE to reimburse the manufacturer for an amount equal to the *sales* tax which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer. The Lemon Law was silent with respect to the BOE reimbursing *use* tax to the manufacturer.

### Brief Summary of Current Lemon Law (inclusive of amendments made by AB 242)

#### *Civil Code section 1793.2*

Civil Code section 1793.2 provides, in relevant part, that if a manufacturer or its representative in this state, such as an authorized dealer, is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer is required to either promptly replace the vehicle or make restitution to the buyer. (Civ. Code § 1793.2(d)(2).)

In the case of restitution, subparagraph (d)(2)(B) provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer, including any collateral charges such as sales or use tax. When restitution is made, the amount to be paid by the manufacturer to the buyer may be reduced by that amount directly attributable to use by the buyer prior to the time the buyer first delivered the vehicle for correction of the problem. (Civ. Code § 1793.2(d)(2)(C).) Subparagraph (d)(2)(D) further specifies that “pursuant to Section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

#### *Civil Code section 1793.25*

Civil Code section 1793.25 provides, in relevant part, that the BOE shall reimburse a manufacturer for an amount equal to the sales or use tax which the manufacturer (1) pays to or for a buyer or lessee when providing a replacement vehicle, or (2) includes in making restitution to the buyer or lessee, subject to satisfactory proof, as specified. (Civ. Code § 1793.25(a).)

**FORMAL ISSUE PAPER 13-012**

A manufacturer is required to provide satisfactory proof that it complied with Civil Code subdivision 1793.23(c), which pertains to inscribing the ownership certificate with the notation “Lemon Law Buyback” and affixing a decal to the vehicle, and satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle has paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of that motor vehicle. (Civ. Code § 1793.25(a).)

The amount of use tax that the State Board of Equalization is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee. (Civ. Code § 1793.25(e).)

## **V. Discussion**

### Amendments to Civil Code sections 1793.2 and 1793.25

AB 242 made amendments to Civil Code sections 1793.2 and 1793.25 to make clear that a refund for use tax is also authorized under the Lemon Law. AB 242 also specified that the amendments were declaratory of existing law. For purposes of discussion, a summary of those amendments are as follows:

With respect to Civil Code section 1793.2:

- Amended subparagraph (d)(2)(B) to add “use tax” to the collateral charges which a buyer is entitled to receive in cases of restitution.
- Added subparagraph (d)(2)(D) which specifies that “pursuant to section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

With respect to Civil Code section 1793.25:

- Amended subdivision (a) to specify that the BOE shall reimburse the manufacturer of a new motor vehicle for an amount equal to the sales tax “or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or making restitution under the Lemon Law, and
- Expanded the satisfactory proof required of the manufacturer, under subdivision (a), to include proof that
  - The buyer of the motor vehicle has paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
  - The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of that motor vehicle.
- Added subdivision (e) which specifies that the amount of use tax that BOE is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee.

### Interested Parties Comments

BOE staff conducted an interested parties meeting to discuss the proposed amendments to Regulation 1655 on August 8, 2013. A participant inquired as to how the provisions of Regulation

1655 would apply to a transaction in which a lessor paid tax at the time of purchase of a vehicle for which it would then lease. Staff considered the scenario and subsequent to the meeting, explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement. With respect to sales tax transactions, the existing provisions of Regulation 1655 would apply. Furthermore, it was noted that the application of Regulation 1655 to sales tax transactions is beyond the scope of the current issue of whether to amend Regulation 1655 to clarify the provisions of the Lemon Law applicable to use tax transactions. Since staff did not receive any other inquiries or comments subsequent to the first interested parties meeting and had no changes to its recommendation, the second discussion paper and second interested parties meeting were canceled. Staff notified interested parties that comments may be submitted up to October 17, 2013 for consideration in the preparation of this Formal Issue Paper. Staff did not receive any other comments.

## VI. Alternative 1 - Staff Recommendation

### A. Description of Alternative 1

Regulation 1655, *Returns, Defects and Replacements*, provides guidance with respect to the tax reimbursement provisions of California's Lemon Law. In light of AB 242, staff recommends that Regulation 1655 be amended to:

- Incorporate the new provision of Civil Code subparagraph 1793.2(d)(2)(D) by specifying that the term buyer includes a lessee of a new motor vehicle. (Proposed amendments to subdivision (b)(2)(A).)
- Add the term "or use" where the current regulation refers to "sales tax or sales tax reimbursement." (Proposed amendments to subdivisions (b)(2)(B) and (b)(2)(C).)
- Add the term "or lease" after "sales" where the current regulation refers to "sales agreement." (Proposed amendments to subdivision (b)(2)(B).)
- Add the term "or lessor" where the current regulation references "dealer" and add the term "or lease" where the current regulation references "retail sale." (Proposed amendments to subdivision (b)(2)(B).)
- Incorporate the provisions of amended Civil Code subdivision 1793.2(a) by expanding the list of evidence required of a manufacturer when filing a claim for refund to include proof that: the buyer of the motor vehicle has paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state; or the lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of that motor vehicle. (Proposed amendments to subdivision (b)(2)(B).)
- Specify that the amount of use tax that BOE is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee, as provided by Civil Code subdivision 1793.25(e). (Proposed new subdivision (b)(2)(D).)

### B. Pros of Alternative 1

- Ensures that Regulation 1655 is consistent with the amendments made to the Civil Code by AB 242.
- Clarifies that a manufacturer may file a claim for refund for an amount for use tax which the manufacturer paid to or for the buyer under the provisions of the Lemon Law.
- Provides guidance to retailers as to the satisfactory proof required when filing a claim for refund.

**C. Cons of Alternative 1**

None.

**D. Statutory or Regulatory Change for Alternative 1**

No statutory change is required. However, staff's recommendation does require adoption of amendments to Regulation 1655.

**E. Operational Impact of Alternative 1**

Staff will publish the proposed amendments to Regulation 1655 and thereby begin the formal rulemaking process.

**F. Administrative Impact of Alternative 1**

**1. Cost Impact**

The workload associated with publishing the regulation and updating manuals and publications is considered routine. Any corresponding cost associated with these activities would be absorbed within the BOE's existing budget. Staff has noted the number of claims for refund filed pursuant to the Lemon Law has increased by approximately 30 percent. Staff attributes the increase to the amendments made by AB 242 and is still evaluating personnel needs.

**2. Revenue Impact**

None. See Revenue Estimate (Exhibit 1).

**G. Taxpayer/Customer Impact of Alternative 1**

Staff believes the proposed amendments clarify, to taxpayers and staff, that a manufacturer may file a claim for refund for use tax paid to or for a buyer under the Lemon Law. In addition, the amendments specify the type of proof required of a manufacturer when it files a claim for refund.

**H. Critical Time Frames of Alternative 1**

None.

**VII. Other Alternative**

**A. Description of Alternative 2**

Do not amend Regulation 1655.

**B. Pros of Alternative 2**

The BOE would not incur the workload associated with processing the amended regulation.

**C. Cons of Alternative 2**

Regulation 1655 will not be entirely consistent with the amendments made to the Civil Code by AB 242 and, therefore, may cause confusion to taxpayers.

**D. Statutory or Regulatory Changes for Alternative 2**

None.

**E. Operational Impact of Alternative 2**

None.

**F. Administrative Impact of Alternative 2**

**1. Cost Impact**

None.

**2. Revenue Impact**

None. See Revenue Estimate (Exhibit 1).

**G. Taxpayer/Customer Impact of Alternative 2**

Without regulatory amendments, there may be confusion as to whether a manufacturer may file a claim for refund for use tax paid to or for a buyer under the Lemon Law. In addition, there would not be clear guidance as to the type of proof required of a manufacturer when it files a claim for refund.

**H. Critical Time Frames for Alternative 2**

None.

**Preparer/Reviewer Information**

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

Current as of: November 26, 2013

**REVENUE ESTIMATE**

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION



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## **Proposed Amendments to Regulation 1655, Returns, Defects and Replacements**

### **I. Issue**

Whether the Board should amend Sales and Use Tax Regulation (Regulation) 1655, Returns, Defects and Replacements, in order to implement, interpret, and make specific the amendments made to Civil Code sections 1793.2 and 1793.25, by Assembly Bill 242 (AB 242)(Stat. 2011, Ch. 727). These sections require the Board of Equalization (BOE) to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California’s “Lemon Law.” Prior to AB 242, the Lemon Law only required reimbursement of sales tax or sales tax reimbursement.

### **Alternative 1 - Staff Recommendation**

Staff recommends the Board approve and authorize publication of the amendments to Regulation 1655, as set forth in Exhibit 2. Staff’s proposed amendments incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle.
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Expanding the list of evidence required of a manufacturer when filing a claim for refund.
- Specifying that the amount of use tax that BOE is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee.

### **II. Other Alternative Considered**

Do not approve proposed amendments to Regulation 1655.

## **Background, Methodology, and Assumptions**

### **Alternative 1 – Staff Recommendation**

There is nothing in the staff recommendation that would impact revenue. The staff recommendation implements legislation declaratory of existing law. The revenue impact for AB 242 has already been estimated in the Assembly Floor Analysis dated September 7, 2011. Therefore, the proposed amendments to Regulation 1655 do not have a revenue impact.

### **Other Alternatives Considered**

Alternative 2 – Do not approve proposed amendments to Regulation 1655.

There is nothing in Alternative 2 that would impact sales and use tax revenue.

## **Revenue Summary**

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

Alternative 2 – 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. This estimate has been reviewed by Mr. Joe Fitz, Chief, Research and Statistics Section, Legislative and Research Division, and Ms. Susanne Buehler, Chief, Tax Policy Division, Sales and Use Tax Department. For additional information, please contact Mr. Benson at (916) 445-0840.

Current as of November 26, 2013.

**Regulation 1655, Returns, Defects and Replacements**

Reference: Sections 6006-6012 and 6012.3, Revenue and Taxation Code; Sections 1793.2-1793.25, Civil Code; and Sections 11713.12 and 11713.21, Vehicle Code.

(a) Returned Merchandise.

(1) In General. Except as provided in paragraph (2) of this subdivision, the amount upon which tax is computed does not include the amount charged for merchandise returned by customers if, (1) the full sale price, including that portion designated as "sales tax," is refunded either in cash or credit, and (2) the customer, in order to obtain the refund or credit, is not required to purchase other property at a price greater than the amount charged for the property that is returned. Refund or credit of the entire amount is deemed to be given when the purchase price, less rehandling and restocking costs, is refunded or credited to the customer. The amount withheld for rehandling and restocking may not exceed the actual cost of rehandling and restocking the returned merchandise. However, in lieu of using the actual cost for each transaction, the amount withheld for rehandling and restocking may be a percentage of the sales price determined by the average cost of rehandling and restocking returned merchandise during the previous accounting cycle (generally one year). If the seller elects to withhold rehandling and restocking amounts based on a percentage of sales price, the seller is bound by that election for the entire accounting cycle for which the election is made and must apply that percentage in lieu of actual cost during that period on all returned merchandise transactions for which rehandling and restocking costs are withheld. The amount withheld as rehandling and restocking costs may not include compensation for increased overhead costs because of the return, for refinishing or restoring the property to salable condition where the necessity therefore is occasioned by customer usage, or for any expense prior to the "sale" (i.e., transfer of title, lease, or possession under a conditional sale contract). Sellers must maintain adequate records which may be verified by audit, documenting the percentage used.

(2) Contract Cancellation Options Required by Car Buyer's Bill of Rights.

(A) Contract Cancellation Option. On and after July 1, 2006, the terms "gross receipts" and "sales price" do not include the purchase price for a contract cancellation option agreement with respect to a contract to purchase a used vehicle with a purchase price of less than forty thousand dollars (\$40,000), which a dealer is required to offer to a buyer pursuant to Vehicle Code section 11713.21. The purchase price for a contract cancellation option described in this subparagraph shall not exceed:

1. Seventy-five dollars (\$75) for a vehicle with a cash price of five thousand dollars (\$5,000) or less;
2. One hundred fifty dollars (\$150) for a vehicle with a cash price of more than five thousand dollars (\$5,000), but not more than ten thousand dollars (\$10,000);

3. Two hundred fifty dollars (\$250) for a vehicle with a cash price of more than ten thousand dollars (\$10,000), but not more than thirty thousand dollars (\$30,000); or
4. One percent of the purchase price for a vehicle with a cash price of more than thirty thousand dollars (\$30,000), but less than forty thousand dollars (\$40,000).

(B) Restocking Fee. On and after July 1, 2006, the terms "gross receipts" and "sales price" do not include the dollar amount of a restocking fee the buyer must pay to the dealer to exercise the right to cancel a purchase of a used car under a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph. The dollar amount of a restocking fee described in this subparagraph shall not exceed:

1. One hundred seventy-five dollars (\$175) if the vehicle's cash price is five thousand dollars (\$5,000) or less;
2. Three hundred fifty dollars (\$350) if the vehicle's cash price is more than five thousand dollars (\$5,000), but less than ten thousand dollars (\$10,000); or
3. Five hundred dollars (\$500) if the vehicle's cash price is ten thousand dollars (\$10,000) or more.

(C) Amounts Refunded to Customers. On and after July 1, 2006, the terms "gross receipts" and "sales price" do not include that portion of the selling price for a used motor vehicle that is refunded to the buyer due to the buyer's exercise of the right to return the vehicle for a refund, which is contained in a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph.

(b) Defective Merchandise.

(1) In General. Amounts credited or refunded by sellers to consumers on account of defects in merchandise sold may be excluded from the amount on which tax is computed. If, however, defective merchandise is accepted as part payment for other merchandise and an additional allowance or credit is given on account of its defective condition, only the amount allowed or credited on account of defects may be excluded from taxable gross receipts. The amount allowed as the "trade-in" value must be included in the measure of tax.

(2) Restitution or Replacement Under California Lemon Law.

(A) General. Under subdivision (d) of Civil Code section 1793.2, if a manufacturer is unable to service or repair a "new motor vehicle," as that term is defined in subdivision (e)(2) of Civil Code section 1793.22, to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer must either replace the motor vehicle or provide the buyer restitution of the purchase price, less specified amounts, at the buyer's election.

For purposes of this regulation, the term buyer shall include a lessee of a new motor vehicle.

(B) Restitution. A manufacturer who pays a buyer restitution pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 is entitled to a refund of the amount of sales or use tax, or sales tax reimbursement included in the restitution paid by the manufacturer to the buyer. The manufacturer may file a claim for refund of that amount with the Bboard. The claim must include a statement that the claim is submitted in accordance with the provisions of section 1793.25 of the Civil Code. The manufacturer must submit with the claim documents evidencing that restitution was made pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 including: a copy of the original sales or lease agreement between the buyer and the dealer or lessor of the non-conforming motor vehicle; copies of documents showing all deductions made in calculating the amount of restitution paid to the buyer along with full explanations for those deductions, including settlement documents and odometer statements; a copy of the title branded "Lemon Law Buyback" for the non-conforming motor vehicle returned by the buyer; and proof that the decal the manufacturer is required to affix to that motor vehicle has been so affixed in accordance with section 11713.12 of the Vehicle Code. The manufacturer must also submit with the claim the seller's permit number of the dealer or lessor who made the retail sale or lease of the non-conforming motor vehicle to the buyer, and evidence for one of the following:

1. ~~that~~ The dealer had reported and paid sales tax on the gross receipts from that sale; or

2. The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state; or

3. The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer restitution is not relevant for purposes of determining whether restitution has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(C) Replacement. For purposes of this regulation, a manufacturer who, pursuant to subdivision (d)(2) of Civil Code section 1793.2, replaces a non-conforming motor vehicle with a new motor vehicle substantially identical to the motor vehicle replaced is replacing the motor vehicle under the terms of the mandatory warranty. No additional tax is due unless the buyer is required to pay an additional amount to receive the replacement motor vehicle, in which case tax is due measured by the amount of that payment. If an amount is refunded to the customer as part of the exchange of the non-conforming motor vehicle for the replacement motor vehicle, then that amount is regarded as restitution for purposes of this regulation if it satisfies the requirements of subdivision (d)(2) of Civil Code section 1793.2. The manufacturer may file a claim for refund under subdivision

(b)(2)(B) of this regulation for the amount of sales or use tax, or sales tax reimbursement that is included in the amount of that restitution paid by the manufacturer to the buyer. For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer a replacement is not relevant for purposes of determining whether the replacement has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(D) The amount of use tax the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee pursuant to Civil Code section 1793.2.

(c) Replacement Parts -Warranties.

(1) In General -Definitions. "Mandatory Warranty." A warranty is mandatory within the meaning of this regulation when the buyer, as a condition of the sale, is required to purchase the warranty or guaranty contract from the seller. "Optional Warranty." A warranty is optional within the meaning of this regulation when the buyer is not required to purchase the warranty or guaranty contract from the seller, i.e., the buyer is free to contract with anyone he or she chooses.

(2) Mandatory Warranties. The sale of tangible personal property includes the furnishing, pursuant to the guaranty provisions of the contract of sale, or mandatory warranty, of replacement parts or materials, and if the property subject to the warranty is sold at retail, the measure of the tax includes any amount charged for the guaranty or warranty, whether or not separately stated. The sale of the replacement parts and materials to the seller furnishing them thereunder is a sale for resale and not taxable.

(3) Optional Warranties. The person obligated under an optional warranty contract to furnish parts, materials, and labor necessary to maintain the property is the consumer of the materials and parts furnished and tax applies to the sale of such items to that person. If he or she purchased the property for resale or from outside California, without tax paid on the purchase price, he or she must report and pay tax upon the cost of such property to him or her when he or she appropriates it to the fulfillment of the contract of warranty.

(4) Deductibles. A deductible paid by a customer under the terms of a mandatory or optional warranty contract is subject to tax measured by the amount of the deductible allocable to the sale of tangible personal property to the customer. For example, if the itemized sales price of tangible personal property (or the fair retail value if not separately itemized) provided pursuant to a warranty is 50 percent of the total fair retail value of the repairs and the deductible is \$100, 50 percent of that deductible, \$50, would be allocable to the sale of tangible personal property and would be subject to tax, whether the warranty were optional or mandatory. Unless otherwise stated in the warranty contract, when either an optional or a mandatory warranty provides that the customer will pay a deductible towards repairs and services provided under the warranty, the person providing the warranty contract is liable for any tax or tax reimbursement otherwise payable by the customer with respect to that deductible.

BEFORE THE CALIFORNIA STATE BOARD OF EQUALIZATION

450 N STREET

SACRAMENTO, CALIFORNIA

REPORTER'S TRANSCRIPT

DECEMBER 17, 2013

BUSINESS TAXES COMMITTEE

REPORTED BY: Kathleen Skidgel

CSR NO. 9039

P R E S E N T

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For the Committee:

Betty T. Yee  
Chair

Michelle Steel  
Member

Jerome E. Horton  
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 Board of  
Equalization Staff:

Susanne Buehler

Lawrence Mendel

Stephen Smith

---oOo---

1 450 N STREET  
2 SACRAMENTO, CALIFORNIA  
3 DECEMBER 17, 2013

4 ----oOo----

5 MR. HORTON: Ms. Richmond, what is our next  
6 matter?

7 MS. RICHMOND: Our next matter is the  
8 Business Taxes Committee.

9 MR. HORTON: Okay. Let's take a ten-minute  
10 break, Members, and we will return to the Business  
11 Tax Committee.

12 Is that okay, Member Yee?

13 MS. YEE: Yeah.

14 MR. HORTON: All right.

15 (Break taken.)

16 MR. HORTON: Members, let us convene the  
17 meeting of the Board of Equalization.

18 Ms. Richmond, what is our next matter?

19 MS. RICHMOND: Our next matter on today's  
20 agenda is Business Taxes Committee. Ms. Yee is the  
21 Chair of that committee.

22 Ms. Yee.

23 MS. YEE: Thank you, Ms. Richmond.

24 Members, we are convening the Business  
25 Taxes Committee. Two items before the committee  
26 today. The first is proposed amendment to  
27 Regulation 1655 relating to returns, defects and  
28 replacements; and secondly, proposed revisions to

1 Regulation 4902 relating to relief of liability.

2 Let me have Ms. Buehler introduce both  
3 issues.

4 MS. BUEHLER: Good morning. I'm Susanne  
5 Buehler with the Sales and Use Tax Department.

6 We do have two agenda items for your  
7 consideration this morning. We will take each  
8 agenda item and the respective action item  
9 separately before moving to the next.

10 With me for Agenda Item 1 is Mr. Lawrence  
11 Mendel from our Legal Department.

12 For this agenda item, we request your  
13 approval and authorization to publish proposed  
14 amendments to Sales and Use Tax Regulation 1655,  
15 Returns, Defects and Replacements.

16 The proposed amendments clarify that the  
17 Board of Equalization is required to reimburse a  
18 vehicle manufacturer for the use tax that the  
19 manufacturer's required to pay a buyer or lessee  
20 when replacing a vehicle or making restitution under  
21 the Lemon Law.

22 These amendments will ensure the regulation  
23 is consistent with provisions of the Civil Code as  
24 amended by Assembly Bill 242.

25 We are happy to answer any questions you  
26 may have on this topic.

27 MS. YEE: Okay. Thank you, Ms. Buehler.

28 Members? Comments?

1 MR. RUNNER: Move to adopt.

2 MR. HORTON: Second.

3 MS. YEE: Motion by Senator Runner to adopt  
4 the proposed revision that authorized publication.  
5 Second by Mr. Horton.

6 Without objection, that motion carries.

7 Thank you.

8 MS. BUEHLER: Thank you.

9 With me for Agenda Item 2 is Mr. Steve  
10 Smith from our Legal Department.

11 For this agenda item we request your  
12 approval and authorization to publish proposed  
13 amendments to Special Taxes Administration  
14 Regulation 4902, Relief from Liability.

15 The proposed amendments extend relief from  
16 liability to a person who relies on a prior audit of  
17 another person under specific circumstances. A  
18 revision to the proposed amendments has been  
19 recommended subsequent to the distribution of the  
20 issue paper and related materials.

21 At the end of the second paragraph in  
22 subdivision (a) staff proposes that the term "that  
23 person" be revised to "those persons." We  
24 respectfully request that this addition --  
25 additional revision be included as part of the  
26 action item for this item.

27 The proposed amendments, inclusive of the  
28 revision just mentioned, conform Regulation 4902

1 with the revisions to Sales and Use Tax Regulation  
2 1705, Relief from Liability, approved for  
3 publication at the August 13, 2013 Business Taxes  
4 Committee meeting.

5 We are happy to answer any questions you  
6 may have on this topic.

7 MS. YEE: Okay, thank you, Ms. Buehler.  
8 Questions, Members?

9 MR. HORTON: Move to adoption.

10 MS. YEE: Motion by Mr. Horton to adopt the  
11 proposed revision to authorize publications. Is  
12 there a second?

13 MS. STEEL: Second.

14 MS. YEE: Second by Ms. Steel.

15 Without objection, that motion carries.

16 Thank you very much, Members.

17 MS. BUEHLER: Thank you.

18 MS. YEE: And this concludes the Business  
19 Taxes Committee.

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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 December 17, 2013 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 6 constitute a complete and accurate transcription of the shorthand writing.

Dated: January 8, 2013

*Kathleen Skidgel*

KATHLEEN SKIDGEL, CSR #9039

Hearing Reporter



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

**Proposed Amendment of Sales and Use Tax Regulation 1655, Returns, Defects and Replacements**

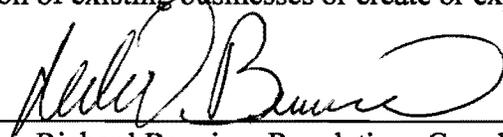
**STATEMENT OF COST OR SAVINGS FOR NOTICE OF PUBLIC HEARING**

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 2/12/14  
Richard Bennion, Regulations Coordinator

Approved by  Date 2/12/14  
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 6615 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. 12/2013)

**ECONOMIC IMPACT STATEMENT**

DEPARTMENT NAME State Board of Equalization	CONTACT PERSON Richard E. Bennion	EMAIL ADDRESS rbennion@boe.ca.gov	TELEPHONE NUMBER 916-445-2130
DESCRIPTIVE TITLE FROM NOTICE REGISTER OR FORM 400 Title 18, Section 1655, Returns, Defects and Replacements			NOTICE FILE NUMBER Z

**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 business 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):

Please see the attached .

***If any box in Items 1 a through g is checked, complete this Economic Impact Statement.  
If box in Item 1.h. is checked, complete the Fiscal Impact Statement as appropriate.***

2. The \_\_\_\_\_ estimates that the economic impact of this regulation (which includes the fiscal impact) is:  
(Agency/Department)

- Below \$10 million
- Between \$10 and \$25 million
- Between \$25 and \$50 million
- Over \$50 million *[If the economic impact is over \$50 million, agencies are required to submit a Standardized Regulatory Impact Assessment as specified in Government Code Section 11346.3(c)]*

3. 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: \_\_\_\_\_

4. Enter the number of businesses that will be created: \_\_\_\_\_ eliminated: \_\_\_\_\_

Explain: \_\_\_\_\_

5. Indicate the geographic extent of impacts:  Statewide  
 Local or regional (List areas): \_\_\_\_\_

6. Enter the number of jobs created: \_\_\_\_\_ and eliminated: \_\_\_\_\_

Describe the types of jobs or occupations impacted: \_\_\_\_\_

7. 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: \_\_\_\_\_

**ECONOMIC AND FISCAL IMPACT STATEMENT  
(REGULATIONS AND ORDERS)**

STD. 399 (REV. 12/2013)

**ECONOMIC IMPACT STATEMENT (CONTINUED)**

**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: \_\_\_\_\_
  - d. Describe other economic costs that may occur: \_\_\_\_\_

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: \$ \_\_\_\_\_

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 of the regulation, which may include among others, the health and welfare of California residents, worker safety and the State's environment: \_\_\_\_\_

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? \$ \_\_\_\_\_

4. Briefly describe any expansion of businesses currently doing business within the State of California that would result from this regulation: \_\_\_\_\_

**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: \_\_\_\_\_

**ECONOMIC AND FISCAL IMPACT STATEMENT  
(REGULATIONS AND ORDERS)**

STD. 399 (REV. 12/2013)

**ECONOMIC IMPACT STATEMENT (CONTINUED)**

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.*

***California Environmental Protection Agency (Cal/EPA) boards, offices and departments are required to submit the following (per Health and Safety Code section 57005). Otherwise, skip to E4.***

1. Will the estimated costs of this regulation to California business enterprises exceed \$10 million?  YES  NO

***If YES, complete E2. and E3  
If NO, skip to E4***

Briefly describe each alternative, or combination of alternatives, for which a cost-effectiveness analysis was performed:

Alternative 1: \_\_\_\_\_

Alternative 2: \_\_\_\_\_

*(Attach additional pages for other alternatives)*

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

Regulation: Total Cost \$ \_\_\_\_\_ Cost-effectiveness ratio: \$ \_\_\_\_\_

Alternative 1: Total Cost \$ \_\_\_\_\_ Cost-effectiveness ratio: \$ \_\_\_\_\_

Alternative 2: Total Cost \$ \_\_\_\_\_ Cost-effectiveness ratio: \$ \_\_\_\_\_

4. Will the regulation subject to OAL review have an estimated economic impact to business enterprises and individuals located in or doing business in California exceeding \$50 million in any 12-month period between the date the major regulation is estimated to be filed with the Secretary of State through 12 months after the major regulation is estimated to be fully implemented?

YES  NO

*If YES, agencies are required to submit a Standardized Regulatory Impact Assessment (SRIA) as specified in Government Code Section 11346.3(c) and to include the SRIA in the Initial Statement of Reasons.*

5. Briefly describe the following:

The increase or decrease of investment in the State: \_\_\_\_\_

The incentive for innovation in products, materials or processes: \_\_\_\_\_

The benefits of the regulations, including, but not limited to, benefits to the health, safety, and welfare of California residents, worker safety, and the state's environment and quality of life, among any other benefits identified by the agency: \_\_\_\_\_

**ECONOMIC AND FISCAL IMPACT STATEMENT  
(REGULATIONS AND ORDERS)**

STD 399 (REV 12/2013)

**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 in the current State Fiscal Year which are reimbursable by the State. (Approximate)  
(Pursuant to Section 6 of Article XIII B of the California Constitution and Sections 17500 et seq. of the Government Code).

\$ \_\_\_\_\_

- a. Funding provided in \_\_\_\_\_  
Budget Act of \_\_\_\_\_ or Chapter \_\_\_\_\_, Statutes of \_\_\_\_\_

- b. Funding will be requested in the Governor's Budget Act of \_\_\_\_\_  
Fiscal Year: \_\_\_\_\_

- 2. Additional expenditures in the current State Fiscal Year which are NOT reimbursable by the State. (Approximate)  
(Pursuant to Section 6 of Article XIII B of the California Constitution and Sections 17500 et seq. of the Government Code).

\$ \_\_\_\_\_

*Check reason(s) this regulation is not reimbursable and provide the appropriate information:*

- a. Implements the Federal mandate contained in \_\_\_\_\_
- b. Implements the court mandate set forth by the \_\_\_\_\_ Court.

Case of: \_\_\_\_\_ vs. \_\_\_\_\_

- c. Implements a mandate of the people of this State expressed in their approval of Proposition No. \_\_\_\_\_  
Date of Election: \_\_\_\_\_

- d. Issued only in response to a specific request from affected local entity(s).  
Local entity(s) affected: \_\_\_\_\_

- e. Will be fully financed from the fees, revenue, etc. from: \_\_\_\_\_  
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;

- g. Creates, eliminates, or changes the penalty for a new crime or infraction contained in \_\_\_\_\_

- 3. Annual Savings. (approximate)  
\$ \_\_\_\_\_

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

- 5. No fiscal impact exists. This regulation does not affect any local entity or program.

- 6. Other. Explain \_\_\_\_\_

**ECONOMIC AND FISCAL IMPACT STATEMENT  
(REGULATIONS AND ORDERS)**

STD. 399 (REV. 12/2013)

**FISCAL IMPACT STATEMENT (CONTINUED)**

**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 in the current State Fiscal Year. (Approximate)

\$ \_\_\_\_\_

It is anticipated that State agencies will:

a. Absorb these additional costs within their existing budgets and resources.

b. Increase the currently authorized budget level for the \_\_\_\_\_ Fiscal Year

2. Savings in the current State Fiscal Year. (Approximate)

\$ \_\_\_\_\_

3. No fiscal impact exists. This regulation does not affect any State agency or program.

4. Other. Explain \_\_\_\_\_

**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 in the current State Fiscal Year. (Approximate)

\$ \_\_\_\_\_

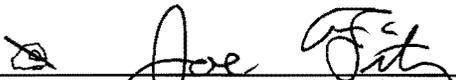
2. Savings in the current State Fiscal Year. (Approximate)

\$ \_\_\_\_\_

3. No fiscal impact exists. This regulation does not affect any federally funded State agency or program.

4. Other. Explain \_\_\_\_\_

FISCAL OFFICER SIGNATURE

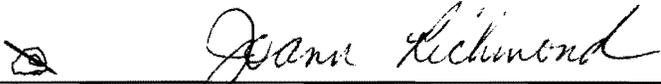


DATE

February 4, 2014

The signature attests that the agency has completed the STD. 399 according to the instructions in SAM sections 6601-6616, 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.

AGENCY SECRETARY



DATE

February 4, 2014

Once approval and signature is required when SAM sections 6601-6616 require completion of Fiscal Impact Statement in the STD. 399.

DEPARTMENT OF FINANCE PROGRAM BUDGET MANAGER

Exempt under SAM section 6615

DATE

**Attachment to Economic and Fiscal Impact**  
**Statement (STD. 399 (Rev. 12/2008)) for the Proposed Amendments to**  
**California Code of Regulations, Title 18, Section 1655,**  
***Returns, Defects and Replacements***

As explained in more detail in the initial statement of reasons, the State Board of Equalization (Board) is currently required under amendments made to Civil Code sections 1793.2 and 1793.25 by Assembly Bill No. 242 (AB 242) (Stat. 2011, ch. 727) to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California's "Lemon Law." Prior to the enactment of AB 242, the Lemon Law only expressly required manufacturers to include sales tax in restitution, and the Board to reimburse a manufacturer for sales tax or sales tax reimbursement included in restitution paid to a buyer. The Lemon Law did not expressly provide that the term buyer includes a lessee, and the Lemon Law did not expressly address the treatment of use tax.

Subdivision (b)(2) of Regulation 1655, *Returns, Defects and Replacements*, explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. The proposed amendments to Regulation 1655 incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).

As a result, the proposed amendments make Regulation 1655 consistent with the amendments made to the Lemon Law by AB 242, the proposed amendments do not mandate that individuals or businesses do anything that is not already required by the Lemon Law, and there is nothing in the proposed amendments that would significantly change how individuals and businesses would generally behave, in the absence of the proposed regulatory action, or that would impose any costs on any persons, including businesses, or impact revenue. Therefore, the Board estimates that the proposed amendments will not have a measurable economic impact on individuals and business that is in addition to whatever economic impact the amendments made to the Lemon Law by AB 242 have had and will have on individuals and businesses. The Board has determined that the proposed amendments to Regulation 1655 are not a major regulation, as defined in Government Code section 11342.548 and California Code of Regulations, title 1, section 2000, because the Board has estimated that the proposed amendments will not have an

economic impact on California business enterprises and individuals in an amount exceeding fifty million dollars (\$50,000,000) during any 12-month period. And, the Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

Therefore, based upon the foregoing information and all of the information in the rulemaking file, 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, and the Board has determined that the proposed amendments to Regulation 1655:

- 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, cost to any 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.

Finally, Regulation 1655 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 1655 will not affect the benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

**NOTICE PUBLICATION/REGULATIONS SUBMISSION**

(See instructions on reverse)

For use by Secretary of State only

STD. 400 (REV. 01-2013)

OAL FILE NUMBERS	NOTICE FILE NUMBER <b>Z-14-0204-03</b>	REGULATORY ACTION NUMBER	EMERGENCY NUMBER
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For use by Office of Administrative Law (OAL) only

<p><b>RECEIVED FOR FILING PUBLICATION DATE</b></p> <p>FEB 04 '14      FEB 14 '14</p> <p><b>Office of Administrative Law</b></p>	<p><b>REGULATIONS</b></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 Returns, Defects and Replacements		TITLE(S) 18	FIRST SECTION AFFECTED 1655	2. REQUESTED PUBLICATION DATE February 14, 2014
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
<b>OAL USE ONLY</b>	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)
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2. SPECIFY CALIFORNIA CODE OF REGULATIONS TITLE(S) AND SECTION(S) (Including title 26, if toxics related)

<b>SECTION(S) AFFECTED</b> (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 January 1, April 1, July 1, or October 1 (Gov. Code §11343.4(a))	<input type="checkbox"/> Effective on filing with Secretary of State	<input 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)

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 1655, *Returns, Defects and Replacements***

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) 1655, *Returns, Defects and Replacements*, which incorporate and implement, interpret, and make specific amendments made to Civil Code sections 1793.2 and 1793.25, by Assembly Bill No. 242 (AB 242) (Stats. 2011, ch. 727). The amendments to these sections require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California's "Lemon Law."

The proposed amendments to Regulation 1655, subdivision (b)(2)(A) incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D) by specifying that the term buyer includes a lessee of a new motor vehicle. The proposed amendments to Regulation 1655, subdivisions (b)(2)(B) and (C) add "or use" tax where the current regulation refers to "sales tax or sales tax reimbursement." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add "or lease" after "sales" where the current regulation refers to "sales agreement" and after "sale" where the current regulation refers to "retail sale." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add "or lessor" after "dealer" where the current regulation refers to "the buyer and the dealer" and "the seller's permit number of the dealer." The proposed amendments revise and reformat the last sentence in Regulation 1655, subdivision (b)(2)(B) to require a manufacturer, when filing a claim for refund, to include "evidence of one of the following" from a list of proof that: (1) "The dealer had reported and paid sales tax on the gross receipts from that sale"; (2) "The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state"; or (3) "The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle." The proposed amendments also add a new subdivision (b)(2)(D) to Regulation 1655 to specify that "The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee," as provided by Civil Code section 1793.25, subdivision (e).

PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on April 22-24, 2014. The Board will provide notice of the meeting to any person who

requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on April 22, 2014. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1655.

## AUTHORITY

RTC section 7051

## REFERENCE

RTC sections 6006-6012, and 6012.3; Civil Code sections 1793.2-1793.25; Vehicle Code sections 11713.12 and 11713.21

## INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

### Current Law

#### *General*

The Song-Beverly Consumer Warranty Act (commencing with Civ. Code, § 1790) contains provisions that provide warranty protections to purchasers of both new and used consumer goods. The act includes provisions (Civ. Code §§ 1793.2 - 1793.26) that require compensation to California consumers of defective new motor vehicles – provisions commonly referred to as California's "Lemon Law." The Lemon Law provides, in relevant part, that if a manufacturer or its representative in this state, such as an authorized dealer, is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer is required to either promptly replace the vehicle or make restitution to the buyer. (Civ. Code, § 1793.2, subd. (d)(2).)

Under the existing Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.), a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant here, a "sale" and a "purchase." (Rev. & Tax. Code, §§ 6006, 6010.) For a lease that is a "sale" and a "purchase," the tax is measured by the rentals payable. However, as provided in subdivision (c)(1) of Regulation 1660, *Leases of Tangible Personal Property – In General*, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686, *Receipts for Tax Paid to Retailers*. The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

The Lemon Law originally provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other collateral charges, *sales* tax. (Civ. Code, § 1793.2.) The Lemon Law further required the Board to reimburse the manufacturer for an amount equal to the *sales* tax which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer when satisfactory proof was provided that the retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale, and that the manufacturer had complied with the requirements of Civil Code section 1793.23, subdivision (c). However, the Lemon Law was silent with respect to whether restitution was required to include *use* tax and whether the Board was required to reimburse a manufacturer for use tax paid to or for a buyer or lessee or included in restitution paid to a buyer or lessee.

As relevant here, AB 242 amended the Lemon Law, specifically Civil Code sections 1793.2 and 1793.25, to make technical corrections sponsored by the Board. The amendments clarify that restitution, under the Lemon Law, includes *use* tax paid or payable by a buyer, including a lessee, of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to the Lemon Law. And, AB 242 provides that the Board-sponsored amendments to the Lemon Law are declaratory of existing law. (AB 242, § 21.)

In the case of restitution, Civil Code section 1793.2, subdivision (d)(2)(B) now provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer, including any collateral charges “such as sales or use tax.” And, Civil Code section 1793.2, subdivision (d)(2)(D) now specifies that “Pursuant to Section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

With respect to reimbursement, Civil Code section 1793.25, subdivision (a) now expressly requires the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to “the sales tax or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or includes in making restitution to the buyer “or lessee” under the Lemon Law, and, as a condition to receiving reimbursement, requires a manufacturer to provide satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of that motor vehicle.

Also, Civil Code section 1793.25, subdivision (e) now provides that “The amount of use tax that the State Board of Equalization is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee” under the Lemon Law.

### Effect, Objective, and Benefits of the Proposed Amendments to Regulation 1655

#### *Need for Clarification*

Subdivision (b)(2) of Regulation 1655 explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. However, Regulation 1655 does not indicate that AB 242 clarified that, under the Lemon Law, restitution includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle and required the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or includes in making restitution to a buyer or lessee, under the Lemon Law. Therefore, the Board’s Business Taxes Committee (BTC) staff determined that amendments to Regulation 1655 are needed in order to make the regulation consistent with and implement, interpret, and make specific AB 242’s amendments to the Lemon Law set forth above.

#### *Interested Parties Process*

As a result of AB 242, BTC staff drafted amendments to Regulation 1655. Specifically, the draft amendments suggested adding language to Regulation 1655, subdivision (b)(2)(A) to incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D), by specifying that, for purposes of Regulation 1655, the term buyer includes a lessee of a new motor vehicle. The draft amendments suggested adding “or use” tax to where the current regulation refers to “sales tax or sales tax reimbursement” in subdivision (b)(2)(B) and (C). The draft amendments suggested adding “or lease” after “sales” where the current regulation refers to “sales agreement” and after “sale” where the current regulation refers to “retail sale” in subdivision (b)(2)(B). The draft amendments also suggested adding “or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer” in subdivision (b)(2)(B).

In addition, the draft amendments suggested revising and reformatting the last sentence in Regulation 1655, subdivision (b)(2)(B), which currently requires a manufacturer, when filing a claim for refund for sales tax or sales tax reimbursement included in restitution paid to a buyer, to submit evidence that the dealer who made the retail sale of the non-conforming vehicle to that buyer reported and paid sales tax on the gross receipts from that sale. The revised and reformatted sentence requires a manufacturer, when filing a claim for refund for sales or use tax or sales tax reimbursement included in restitution

paid to a buyer, including a lessee, under the Lemon Law, to provide “evidence of one of the following” from a list that includes proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The draft amendments also suggested adding a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

BTC staff subsequently prepared a discussion paper regarding the amendments made to the Lemon Law by AB 242 and staff’s draft amendments to Regulation 1655, provided the discussion paper and its draft amendments to Regulation 1655 to the interested parties, and conducted an interested parties meeting on August 8, 2013, to discuss the draft amendments to Regulation 1655. During the interested parties meeting, a participant inquired as to how the provisions of Regulation 1655 would apply to a transaction in which a lessor paid tax at the time the lessor purchased a vehicle which the lessor would then lease. Staff considered the scenario and, subsequent to the meeting, staff explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement from the lessor. (See Reg. 1660, subd. (c)(2) and (3), regarding property purchased tax-paid and leased in substantially the same form as acquired.) And, staff explained that, with respect to sales tax transactions, the existing provisions of Regulation 1655 would apply to a manufacturer’s claim for a refund for sales tax reimbursement the manufacturer included in restitution paid to a lessor, under the Lemon Law. Furthermore, staff noted that AB 242 did not change the application of the Lemon Law to sales tax transactions, and that questions regarding the application of Regulation 1655 to sales tax transactions were beyond the scope of the current interested parties process, which was to discuss the issue of whether to amend Regulation 1655 to clarify the new provisions of the Lemon Law applicable to use tax transactions.

Since BTC staff did not receive any other inquiries or comments regarding its draft amendments during or subsequent to the first interested parties meeting and staff had no changes to its recommendation to amend Regulation 1655, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff’s draft amendments. Staff also notified interested parties that comments could be submitted up to October 17, 2013, for consideration in the preparation of a Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

#### *December 17, 2013, BTC Meeting*

Subsequently, staff prepared Formal Issue Paper 13-012 and distributed it to the Board Members for consideration at the Board’s December 17, 2013, BTC meeting. Formal Issue Paper 13-012 recommended that the Board approve and authorize publication of the

amendments to Regulation 1655 (discussed above) in order to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).

During the December 17, 2013, BTC meeting, the Board Members unanimously voted to propose the amendments to Regulation 1655 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1655 are reasonably necessary to have the effect and accomplish the objective of making the regulation consistent with and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1655 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 1655 is the only state regulation prescribing the requirements for the Board to reimburse a manufacturer under Civil Code section 1793.25. In addition, the Board has determined that there are no comparable federal regulations or statutes to Regulation 1655 or the proposed amendments to Regulation 1655.

#### NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will result in no direct or indirect cost or savings to any state agency, cost to any local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

## NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The Board has made an initial determination that the adoption of the proposed amendments to Regulation 1655 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 1655 may affect small business.

## NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

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

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

The Board has prepared the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will not affect the benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

## NO SIGNIFICANT EFFECT ON HOUSING COSTS

The adoption of the proposed amendments to Regulation 1655 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 Monica Gonzalez Silva, Tax Counsel III, by telephone at (916) 323-3138, by e-mail at [Monica.Silva@boe.ca.gov](mailto:Monica.Silva@boe.ca.gov), or by mail at State Board of Equalization, Attn: Monica Gonzalez Silva, 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](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

#### WRITTEN COMMENT PERIOD

The written comment period ends at 10:00 a.m. on April 22, 2014, or as soon thereafter as the Board begins the public hearing regarding the adoption of the proposed amendments to Regulation 1655 during the April 22-24, 2014, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1655. 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 1655 illustrating the express terms of the proposed amendments. The Board has also prepared an initial statement of reasons for the adoption of the proposed amendments to Regulation 1655, which includes the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

#### SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The Board may adopt the proposed amendments to Regulation 1655 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed regulation, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting regulation will be mailed to those interested parties who commented on the original proposed regulation orally or in writing or who asked to be informed of such changes. The text of the resulting regulation will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting regulation that are received prior to adoption.

#### AVAILABILITY OF FINAL STATEMENT OF REASONS

If the Board adopts the proposed amendments to Regulation 1655, 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](http://www.boe.ca.gov).

## Bennion, Richard

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**From:** BOE-Board Meeting Material  
**Sent:** Friday, February 14, 2014 9:56 AM  
**To:** Alonzo, Mary Ann (Legal); Angeja, Jeff (Legal); Angeles, Joel; Appleby, Jaclyn; Armenta, Christopher; Baetge, Michelle; Bartolo, Lynn; Bennion, Richard; Benson, Bill; Bisauta, Christine (Legal); Blake, Sue; BOE-Board Meeting Material; Boyle, Kevin; Bridges, Cynthia; Brown, Michele C; Chung, Sophia (Legal); Cruz, Giovan; Davis, Toya P.; Delgado, Maria; Dixon, Camille; Duran, David; Elliott, Claudia; Epolite, Anthony (Legal); Ferris, Randy (Legal); Ford, Ladeena L; Garcia, Laura; Gau, David; Gilman, Todd; Goehring, Teresa; Hale, Mike; Hamilton, Tabitha; Hanohano, Rebecca; Harvill, Mai; He, Mengjun; Heller, Bradley (Legal); Hellmuth, Leila; Herrera, Cristina; Holmes, Dana; Hughes, Shellie L; Jacobson, Andrew; Kinkle, Sherrie L; Kinst, Lynne; Kruckenberg, Kendra; Kuhl, James; Lambert, Gary; Lambert, Robert (Legal); Lee, Chris; Levine, David H. (Legal); LoFaso, Alan; Madrigal, Claudia; Mandel, Marcy Jo; Matsumoto, Sid; McGuire, Jeff; Miller, Brad; Mandel, Marcy Jo @ SCO; Moon, Richard (Legal); Morquecho, Raymond; Nienow, Trecia (Legal); Oakes, Clifford; Pielsticker, Michele; Ralston, Natasha; Richmond, Joann; Riley, Denise (Legal); Salazar, Ramon; Salgado-Ponce, Sylvia; Schultz, Glenna; Shah, Neil; Silva, Monica (Legal); Singh, Sam; Smith, Kevin (Legal); Smith, Rose; Stowers, Yvette; Suero-Gabler, Cynthia; Torres, Rodrigo; Torres, Rodrigo; Tran, Mai (Legal); Treichelt, Tim; Tucker, Robert (Legal); Vandrlick, Tanya; Vasquez, Rosalyn; Vigil, Michael; Wallentine, Sean; Whitaker, Lynn; White, Sharon; Williams, Lee; Zivkovich, Robert  
**Subject:** State Board of Equalization - Announcement of Regulatory Change 1655

The State Board of Equalization proposes to adopt amendments to Regulation 1655, *Returns, Defects and Replacements*. 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 April 22-24, 2014.

The proposed amendments to Regulation 1655, *Returns, Defects and Replacements*, clarify that the regulation's provisions regarding restitution and replacement under the "Lemon Law" apply to use tax under specified circumstances.

To view the notice of hearing, initial statement of reasons, proposed text, and history click on the following link:  
[http://www.boe.ca.gov/regs/reg\\_1655\\_2014.htm](http://www.boe.ca.gov/regs/reg_1655_2014.htm).

Questions regarding the substance of the proposed amendments should be directed to Ms. Monica Silva, Tax Counsel III, at 450 N Street, MIC:82, Sacramento, CA 94279-0082, email [Monica.Silva@boe.ca.gov](mailto:Monica.Silva@boe.ca.gov), telephone (916) 323-3138, 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](mailto: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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Please do not reply to this message.

Board Proceedings Division, MIC:80  
Rick Bennion  
Regulations Coordinator  
Phone (916) 445-2130

## **Bennion, Richard**

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**From:** State Board of Equalization - Announcement of Regulatory Change  
<Legal.Regulations@BOE.CA.GOV>  
**Sent:** Friday, February 14, 2014 11:00 AM  
**To:** BOE\_REGULATIONS@LISTSERV.STATE.CA.GOV  
**Subject:** State Board of Equalization - Announcement of Regulatory Change 1655

The State Board of Equalization proposes to adopt amendments to Regulation 1655, *Returns, Defects and Replacements*. 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 April 22-24, 2014.

The proposed amendments to Regulation 1655, *Returns, Defects and Replacements*, clarify that the regulation's provisions regarding restitution and replacement under the "Lemon Law" apply to use tax under specified circumstances.

To view the notice of hearing, initial statement of reasons, proposed text, and history click on the following link:  
[http://www.boe.ca.gov/regs/reg\\_1655\\_2014.htm](http://www.boe.ca.gov/regs/reg_1655_2014.htm).

Questions regarding the substance of the proposed amendments should be directed to Ms. Monica Silva, Tax Counsel III, at 450 N Street, MIC:82, Sacramento, CA 94279-0082, email [Monica.Silva@boe.ca.gov](mailto:Monica.Silva@boe.ca.gov), telephone (916) 323-3138, 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](mailto: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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**CONSIDERATION OF ALTERNATIVES**

The Board must determine that no reasonable alternative it considered to the regulation or that has otherwise been 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 proposal described in this Notice, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law.

Any interested person may present statements or arguments orally or in writing relevant to the above determinations at the above-mentioned hearing.

**INITIAL STATEMENT OF REASONS AND INFORMATION**

The Board has prepared an initial statement of the reasons for the proposed action and has available all the information upon which the proposal is based.

**TEXT OF PROPOSAL**

Copies of the exact language of the proposed regulations, and any document incorporated by reference, and of the initial statement of reasons, and all of the information upon which the proposal is based, may be obtained at the hearing or prior to the hearing upon request from the California Architects Board at 2420 Del Paso Road, Suite 105, Sacramento, California 95834 or by telephoning the contact person listed below.

**AVAILABILITY AND LOCATION OF THE FINAL STATEMENT OF REASONS AND RULEMAKING FILE**

All the information upon which the proposed regulations are based is contained in the rulemaking file which is available for public inspection by contacting the person named below.

You may obtain a copy of the final statement of reasons once it has been prepared, by making a written request to the contact person named below (or by accessing the website listed below).

**CONTACT PERSON**

Inquiries or comments concerning the proposed rule-making action may be addressed to:

Name: Timothy Rodda  
Address: 2420 Del Paso Road, Suite 105  
Sacramento, CA 95834  
Telephone No.: (916) 575-7217  
Fax No.: (916) 575-7283  
E-Mail Address: timothy.rodde@dca.ca.gov

The backup contact person is:

Name: Marccus Reinhardt  
Address: 2420 Del Paso Road, Suite 105  
Sacramento, CA 95834  
Telephone No.: (916) 575-7212  
Fax No.: (916) 575-7283  
E-Mail Address: marccus.reinhardt@dca.ca.gov

Website Access: Materials regarding this proposal can be found at [www.cab.ca.gov](http://www.cab.ca.gov).

**TITLE 18. BOARD OF EQUALIZATION**

**The State Board of Equalization Proposes to Adopt Amendments to California Code of Regulations, Title 18, Section 1655, Returns, Defects and Replacements**

**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) 1655, *Returns, Defects and Replacements*, which incorporate and implement, interpret, and make specific amendments made to Civil Code sections 1793.2 and 1793.25, by Assembly Bill No. 242 (AB 242) (Stats. 2011, ch. 727). The amendments to these sections require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California's "Lemon Law."

The proposed amendments to Regulation 1655, subdivision (b)(2)(A) incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D) by specifying that the term buyer includes a lessee of a new motor vehicle. The proposed amendments to Regulation 1655, subdivisions (b)(2)(B) and (C) add "or use" tax where the current regulation refers to "sales tax or sales tax reimbursement." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add "or lease" after "sales" where the current regulation refers to "sales agreement" and after "sale" where the current regulation refers to "retail sale." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add

“or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer.” The proposed amendments revise and reformat the last sentence in Regulation 1655, subdivision (b)(2)(B) to require a manufacturer, when filing a claim for refund, to include “evidence of one of the following” from a list of proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) “The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The proposed amendments also add a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

PUBLIC HEARING

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on April 22–24, 2014. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board’s Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on April 22, 2014. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1655.

AUTHORITY

RTC section 7051

REFERENCE

RTC sections 6006–6012, and 6012.3; Civil Code sections 1793.2–1793.25; Vehicle Code sections 11713.12 and 11713.21

INFORMATIVE DIGEST/POLICY STATEMENT  
OVERVIEW

Current Law

*General*

The Song–Beverly Consumer Warranty Act (commencing with Civ. Code, § 1790) contains provisions that provide warranty protections to purchasers of both

new and used consumer goods. The act includes provisions (Civ. Code §§ 1793.2–1793.26) that require compensation to California consumers of defective new motor vehicles — provisions commonly referred to as California’s “Lemon Law.” The Lemon Law provides, in relevant part, that if a manufacturer or its representative in this state, such as an authorized dealer, is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer is required to either promptly replace the vehicle or make restitution to the buyer. (Civ. Code, § 1793.2, subd. (d)(2).)

Under the existing Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.), a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant here, a “sale” and a “purchase.” (Rev. & Tax. Code, §§ 6006, 6010.) For a lease that is a “sale” and a “purchase,” the tax is measured by the rentals payable. However, as provided in subdivision (c)(1) of Regulation 1660, *Leases of Tangible Personal Property — In General*, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686, *Receipts for Tax Paid to Retailers*. The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

The Lemon Law originally provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other collateral charges, *sales tax*. (Civ. Code, § 1793.2.) The Lemon Law further required the Board to reimburse the manufacturer for an amount equal to the *sales tax* which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer when satisfactory proof was provided that the retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale, and that the manufacturer had complied with the requirements of Civil Code section 1793.23, subdivision (c). However, the Lemon Law was silent with respect to whether restitution was required to include use tax and whether the Board was required to reimburse a manufacturer for use tax paid to or for a buyer or lessee or included in restitution paid to a buyer or lessee.

As relevant here, AB 242 amended the Lemon Law, specifically Civil Code sections 1793.2 and 1793.25, to make technical corrections sponsored by the Board. The amendments clarify that restitution, under the Lemon Law, includes *use tax* paid or payable by a buyer, including a lessee, of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use tax* that the

manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to the Lemon Law. And, AB 242 provides that the Board-sponsored amendments to the Lemon Law are declaratory of existing law. (AB 242, §21.)

In the case of restitution, Civil Code section 1793.2, subdivision (d)(2)(B) now provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer, including any collateral charges “such as sales or use tax.” And, Civil Code section 1793.2, subdivision (d)(2)(D) now specifies that “Pursuant to Section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

With respect to reimbursement, Civil Code section 1793.25, subdivision (a) now expressly requires the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to “the sales tax or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or includes in making restitution to the buyer “or lessee” under the Lemon Law, and, as a condition to receiving reimbursement, requires a manufacturer to provide satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of that motor vehicle.

Also, Civil Code section 1793.25, subdivision (e) now provides that “The amount of use tax that the State Board of Equalization is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee” under the Lemon Law.

Effect, Objective, and Benefits of the Proposed Amendments to Regulation 1655

*Need for Clarification*

Subdivision (b)(2) of Regulation 1655 explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. However, Regulation 1655 does not indicate that AB 242 clarified that, under the Lemon Law, restitution includes use tax paid or payable by a buyer or lessee of a

new motor vehicle and required the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or includes in making restitution to a buyer or lessee, under the Lemon Law. Therefore, the Board’s Business Taxes Committee (BTC) staff determined that amendments to Regulation 1655 are needed in order to make the regulation consistent with and implement, interpret, and make specific AB 242’s amendments to the Lemon Law set forth above.

*Interested Parties Process*

As a result of AB 242, BTC staff drafted amendments to Regulation 1655. Specifically, the draft amendments suggested adding language to Regulation 1655, subdivision (b)(2)(A) to incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D), by specifying that, for purposes of Regulation 1655, the term buyer includes a lessee of a new motor vehicle. The draft amendments suggested adding “or use” tax where the current regulation refers to “sales tax or sales tax reimbursement” in subdivision (b)(2)(B) and (C). The draft amendments suggested adding “or lease” after “sales” where the current regulation refers to “sales agreement” and after “sale” where the current regulation refers to “retail sale” in subdivision (b)(2)(B). The draft amendments also suggested adding “or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer” in subdivision (b)(2)(B).

In addition, the draft amendments suggested revising and reformatting the last sentence in Regulation 1655, subdivision (b)(2)(B), which currently requires a manufacturer, when filing a claim for refund for sales tax or sales tax reimbursement included in restitution paid to a buyer, to submit evidence that the dealer who made the retail sale of the nonconforming vehicle to that buyer reported and paid sales tax on the gross receipts from that sale. The revised and reformatted sentence requires a manufacturer, when filing a claim for refund for sales or use tax or sales tax reimbursement included in restitution paid to a buyer, including a lessee, under the Lemon Law, to provide “evidence of one of the following” from a list that includes proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) “The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The draft amendments also suggested adding a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount

of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

BTC staff subsequently prepared a discussion paper regarding the amendments made to the Lemon Law by AB 242 and staff’s draft amendments to Regulation 1655, provided the discussion paper and its draft amendments to Regulation 1655 to the interested parties, and conducted an interested parties meeting on August 8, 2013, to discuss the draft amendments to Regulation 1655. During the interested parties meeting, a participant inquired as to how the provisions of Regulation 1655 would apply to a transaction in which a lessor paid tax at the time the lessor purchased a vehicle which the lessor would then lease. Staff considered the scenario and, subsequent to the meeting, staff explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement from the lessor. (See Reg. 1660, subd. (c)(2) and (3), regarding property purchased tax-paid and leased in substantially the same form as acquired.) And, staff explained that, with respect to sales tax transactions, the existing provisions of Regulation 1655 would apply to a manufacturer’s claim for a refund for sales tax reimbursement the manufacturer included in restitution paid to a lessor, under the Lemon Law. Furthermore, staff noted that AB 242 did not change the application of the Lemon Law to sales tax transactions, and that questions regarding the application of Regulation 1655 to sales tax transactions were beyond the scope of the current interested parties process, which was to discuss the issue of whether to amend Regulation 1655 to clarify the new provisions of the Lemon Law applicable to use tax transactions.

Since BTC staff did not receive any other inquiries or comments regarding its draft amendments during or subsequent to the first interested parties meeting and staff had no changes to its recommendation to amend Regulation 1655, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff’s draft amendments. Staff also notified interested parties that comments could be submitted up to October 17, 2013, for consideration in the preparation of a Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

*December 17, 2013, BTC Meeting*

Subsequently, staff prepared Formal Issue Paper 13–012 and distributed it to the Board Members for consideration at the Board’s December 17, 2013, BTC meeting. Formal Issue Paper 13–012 recommended that the Board approve and authorize publication of the

amendments to Regulation 1655 (discussed above) in order to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).

During the December 17, 2013, BTC meeting, the Board Members unanimously voted to propose the amendments to Regulation 1655 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1655 are reasonably necessary to have the effect and accomplish the objective of making the regulation consistent with and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1655 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 1655 is the only state regulation prescribing the requirements for the Board to reimburse a manufacturer under Civil Code section 1793.25. In addition, the Board has determined that there are no comparable federal regulations or statutes to Regulation 1655 or the proposed amendments to Regulation 1655.

**NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will result in no direct or indirect cost or savings to any state agency, cost to any local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

**NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS**

The Board has made an initial determination that the adoption of the proposed amendments to Regulation 1655 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 1655 may affect small business.

**NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES**

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

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

The Board has prepared the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will not affect the benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

**NO SIGNIFICANT EFFECT ON HOUSING COSTS**

The adoption of the proposed amendments to Regulation 1655 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 Monica Gonzalez Silva, Tax Counsel III, by telephone at (916) 323-3138, by e-mail at [Monica.Silva@boe.ca.gov](mailto:Monica.Silva@boe.ca.gov), or by mail at State Board of Equalization, Attn: Monica Gonzalez Silva, 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](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

**WRITTEN COMMENT PERIOD**

The written comment period ends at 10:00 a.m. on April 22, 2014, or as soon thereafter as the Board begins the public hearing regarding the adoption of the pro-

posed amendments to Regulation 1655 during the April 22–24, 2014, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1655. 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 1655 illustrating the express terms of the proposed amendments. The Board has also prepared an initial statement of reasons for the adoption of the proposed amendments to Regulation 1655, which includes the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

**SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8**

The Board may adopt the proposed amendments to Regulation 1655 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed regulation, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting regulation will be mailed to those interested parties who commented on the original proposed regulation orally or in writing or who asked to be informed of such changes. The text of the resulting regulation will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting regulation that are received prior to adoption.

**AVAILABILITY OF FINAL STATEMENT OF REASONS**

If the Board adopts the proposed amendments to Regulation 1655, 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](http://www.boe.ca.gov).

**OAL REGULATORY DETERMINATIONS**

**OFFICE OF ADMINISTRATIVE LAW**

**DETERMINATIONS OF ALLEGED UNDERGROUND REGULATIONS (Summary Dispositions)**

**(Pursuant to Government Code Section 11340.5 and Title 1, section 270, of the California Code of Regulations)**

The attachments are not being printed for practical reasons or space considerations. However, if you would like to view the attachments please contact Margaret Molina at (916) 324–6044 or [mmolina@oal.ca.gov](mailto:mmolina@oal.ca.gov).

**DEPARTMENT OF CORRECTIONS AND REHABILITATION**

Date: February 3, 2014  
 To: James Allen  
 From: Chapter Two Compliance Unit  
 Subject: **2014 OAL DETERMINATION NO. 3 (S) (CTU2013–1210–01)**  
 (Summary Disposition issued pursuant to Gov. Code, sec. 11340.5; Cal. Code Regs., tit. 1, sec. 270(f))  
 Petition challenging as an underground regulation Folsom State Prison Gate Pass Clearance Criteria

On December 10, 2013, the Office of Administrative Law (OAL) received your petition asking for a determination as to whether the Folsom State Prison Gate Pass Clearance Criteria (Gate Pass Clearance) constitutes an underground regulation. The rule is in Folsom State Prison D.O.M. Supplement 62010.7.4, dated April 2013. This Gate Pass Clearance criteria was issued by the warden at the Folsom State Prison and is attached hereto as Exhibit A.



STATE OF CALIFORNIA

**STATE BOARD OF EQUALIZATION**

50 N STREET, SACRAMENTO, CALIFORNIA  
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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

CYNTHIA BRIDGES  
Executive Director

**February 14, 2014**

**To Interested Parties:**

**Notice of Proposed Regulatory Action**

**The State Board of Equalization Proposes to Adopt Amendments to  
California Code of Regulations, Title 18,  
Section 1655, *Returns, Defects and Replacements***

**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) 1655, *Returns, Defects and Replacements*, which incorporate and implement, interpret, and make specific amendments made to Civil Code sections 1793.2 and 1793.25, by Assembly Bill No. 242 (AB 242) (Stats. 2011, ch. 727). The amendments to these sections require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California's "Lemon Law."

The proposed amendments to Regulation 1655, subdivision (b)(2)(A) incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D) by specifying that the term buyer includes a lessee of a new motor vehicle. The proposed amendments to Regulation 1655, subdivisions (b)(2)(B) and (C) add "or use" tax where the current regulation refers to "sales tax or sales tax reimbursement." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add "or lease" after "sales" where the current regulation refers to "sales agreement" and after "sale" where the current regulation refers to "retail sale." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add "or lessor" after "dealer" where the current regulation refers to "the buyer and the dealer" and "the seller's permit number of the dealer." The proposed amendments revise and reformat the last sentence in Regulation 1655, subdivision (b)(2)(B) to require a manufacturer, when filing a claim for refund, to include "evidence of one of the following" from a list of proof that: (1) "The dealer had reported and paid sales tax on the

gross receipts from that sale”; (2) ”The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) “The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The proposed amendments also add a new subdivision (b)(2)(D) to Regulation 1655 that specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

## **PUBLIC HEARING**

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on April 22-24, 2014. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board’s Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on April 22, 2014. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1655.

## **AUTHORITY**

RTC section 7051

## **REFERENCE**

RTC sections 6006-6012, and 6012.3; Civil Code sections 1793.2-1793.25; Vehicle Code sections 11713.12 and 11713.21

## **INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW**

### Current Law

#### *General*

The Song-Beverly Consumer Warranty Act (commencing with Civ. Code, § 1790) contains provisions that provide warranty protections to purchasers of both new and used consumer goods. The act includes provisions (Civ. Code §§ 1793.2 - 1793.26) that require compensation to California consumers of defective new motor vehicles – provisions commonly referred to as California’s “Lemon Law.” The Lemon Law provides, in relevant part, that if a manufacturer or its representative in this state, such as an authorized dealer, is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer is required to either promptly replace the vehicle or make restitution to the buyer. (Civ. Code, § 1793.2, subd. (d)(2).)

Under the existing Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.), a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant here, a “sale” and a “purchase.” (Rev. & Tax. Code, §§ 6006, 6010.) For a lease that is a “sale” and a “purchase,” the tax is measured by the rentals payable. However, as provided in subdivision (c)(1) of Regulation 1660, *Leases of Tangible Personal Property – In General*, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686, *Receipts for Tax Paid to Retailers*. The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

The Lemon Law originally provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other collateral charges, *sales tax*. (Civ. Code, § 1793.2.) The Lemon Law further required the Board to reimburse the manufacturer for an amount equal to the *sales tax* which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer when satisfactory proof was provided that the retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale, and that the manufacturer had complied with the requirements of Civil Code section 1793.23, subdivision (c). However, the Lemon Law was silent with respect to whether restitution was required to include *use tax* and whether the Board was required to reimburse a manufacturer for use tax paid to or for a buyer or lessee or included in restitution paid to a buyer or lessee.

As relevant here, AB 242 amended the Lemon Law, specifically Civil Code sections 1793.2 and 1793.25, to make technical corrections sponsored by the Board. The amendments clarify that restitution, under the Lemon Law, includes *use tax* paid or payable by a buyer, including a lessee, of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use tax* that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to the Lemon Law. And, AB 242 provides that the Board-sponsored amendments to the Lemon Law are declaratory of existing law. (AB 242, § 21.)

In the case of restitution, Civil Code section 1793.2, subdivision (d)(2)(B) now provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer, including any collateral charges “such as sales or use tax.” And, Civil Code section 1793.2, subdivision (d)(2)(D) now specifies that “Pursuant to Section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

With respect to reimbursement, Civil Code section 1793.25, subdivision (a) now expressly requires the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to “the sales tax or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or includes in making restitution to the buyer “or lessee” under the Lemon Law, and, as a condition to receiving reimbursement, requires a manufacturer to provide satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of that motor vehicle.

Also, Civil Code section 1793.25, subdivision (e) now provides that “The amount of use tax that the State Board of Equalization is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee” under the Lemon Law.

#### Effect, Objective, and Benefits of the Proposed Amendments to Regulation 1655

##### *Need for Clarification*

Subdivision (b)(2) of Regulation 1655 explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. However, Regulation 1655 does not indicate that AB 242 clarified that, under the Lemon Law, restitution includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle and required the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or includes in making restitution to a buyer or lessee, under the Lemon Law. Therefore, the Board’s Business Taxes Committee (BTC) staff determined that amendments to Regulation 1655 are needed in order to make the regulation consistent with and implement, interpret, and make specific AB 242’s amendments to the Lemon Law set forth above.

##### *Interested Parties Process*

As a result of AB 242, BTC staff drafted amendments to Regulation 1655. Specifically, the draft amendments suggested adding language to Regulation 1655, subdivision (b)(2)(A) to incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D), by specifying that, for purposes of Regulation 1655, the term buyer includes a lessee of a new motor vehicle. The draft amendments suggested adding “or use” tax to where the current regulation refers to “sales tax or sales tax reimbursement” in subdivision (b)(2)(B) and (C). The draft amendments suggested adding “or lease” after “sales” where the current regulation refers to “sales agreement” and after “sale” where the current regulation refers to “retail sale” in subdivision (b)(2)(B). The draft amendments also suggested adding “or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer” in subdivision (b)(2)(B).

In addition, the draft amendments suggested revising and reformatting the last sentence in Regulation 1655, subdivision (b)(2)(B), which currently requires a manufacturer, when filing a claim for refund for sales tax or sales tax reimbursement included in restitution paid to a buyer,

to submit evidence that the dealer who made the retail sale of the non-conforming vehicle to that buyer reported and paid sales tax on the gross receipts from that sale. The revised and reformatted sentence requires a manufacturer, when filing a claim for refund for sales or use tax or sales tax reimbursement included in restitution paid to a buyer, including a lessee, under the Lemon Law, to provide “evidence of one of the following” from a list that includes proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The draft amendments also suggested adding a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

BTC staff subsequently prepared a discussion paper regarding the amendments made to the Lemon Law by AB 242 and staff’s draft amendments to Regulation 1655, provided the discussion paper and its draft amendments to Regulation 1655 to the interested parties, and conducted an interested parties meeting on August 8, 2013, to discuss the draft amendments to Regulation 1655. During the interested parties meeting, a participant inquired as to how the provisions of Regulation 1655 would apply to a transaction in which a lessor paid tax at the time the lessor purchased a vehicle which the lessor would then lease. Staff considered the scenario and, subsequent to the meeting, staff explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement from the lessor. (See Reg. 1660, subd. (c)(2) and (3), regarding property purchased tax-paid and leased in substantially the same form as acquired.) And, staff explained that, with respect to sales tax transactions, the existing provisions of Regulation 1655 would apply to a manufacturer’s claim for a refund for sales tax reimbursement the manufacturer included in restitution paid to a lessor, under the Lemon Law. Furthermore, staff noted that AB 242 did not change the application of the Lemon Law to sales tax transactions, and that questions regarding the application of Regulation 1655 to sales tax transactions were beyond the scope of the current interested parties process, which was to discuss the issue of whether to amend Regulation 1655 to clarify the new provisions of the Lemon Law applicable to use tax transactions.

Since BTC staff did not receive any other inquiries or comments regarding its draft amendments during or subsequent to the first interested parties meeting and staff had no changes to its recommendation to amend Regulation 1655, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff’s draft amendments. Staff also notified interested parties that comments could be submitted up to October 17, 2013, for consideration in the preparation of a Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

*December 17, 2013, BTC Meeting*

Subsequently, staff prepared Formal Issue Paper 13-012 and distributed it to the Board Members for consideration at the Board's December 17, 2013, BTC meeting. Formal Issue Paper 13-012 recommended that the Board approve and authorize publication of the amendments to Regulation 1655 (discussed above) in order to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).

During the December 17, 2013, BTC meeting, the Board Members unanimously voted to propose the amendments to Regulation 1655 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1655 are reasonably necessary to have the effect and accomplish the objective of making the regulation consistent with and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1655 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 1655 is the only state regulation prescribing the requirements for the Board to reimburse a manufacturer under Civil Code section 1793.25. In addition, the Board has determined that there are no comparable federal regulations or statutes to Regulation 1655 or the proposed amendments to Regulation 1655.

**NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will result in no direct or indirect cost or savings to any state agency, cost to any local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

**NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS**

The Board has made an initial determination that the adoption of the proposed amendments to Regulation 1655 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 1655 may affect small business.

**NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES**

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

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

The Board has prepared the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will not affect the benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

**NO SIGNIFICANT EFFECT ON HOUSING COSTS**

The adoption of the proposed amendments to Regulation 1655 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 Monica Gonzalez Silva, Tax Counsel III, by telephone at (916) 323-3138, by e-mail at [Monica.Silva@boe.ca.gov](mailto:Monica.Silva@boe.ca.gov), or by mail at State Board of Equalization, Attn: Monica Gonzalez Silva, 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](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

## **WRITTEN COMMENT PERIOD**

The written comment period ends at 10:00 a.m. on April 22, 2014, or as soon thereafter as the Board begins the public hearing regarding the adoption of the proposed amendments to Regulation 1655 during the April 22-24, 2014, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1655. 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 1655 illustrating the express terms of the proposed amendments. The Board has also prepared an initial statement of reasons for the adoption of the proposed amendments to Regulation 1655, which includes the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed

amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

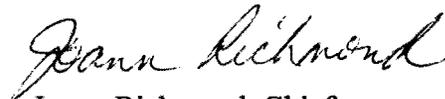
**SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8**

The Board may adopt the proposed amendments to Regulation 1655 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed regulation, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting regulation will be mailed to those interested parties who commented on the original proposed regulation orally or in writing or who asked to be informed of such changes. The text of the resulting regulation will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting regulation that are received prior to adoption.

**AVAILABILITY OF FINAL STATEMENT OF REASONS**

If the Board adopts the proposed amendments to Regulation 1655, 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](http://www.boe.ca.gov)

Sincerely,

  
Joann Richmond, Chief  
Board Proceedings Division

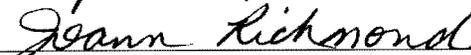
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**STATE BOARD OF EQUALIZATION**



BOARD APPROVED

At the April 22, 2014 Board Meeting

  
\_\_\_\_\_  
Joann Richmond, Chief  
Board Proceedings Division

**Initial Statement of Reasons for  
Proposed Amendments to California Code of Regulations,  
Title 18, Section 1655, *Returns, Defects and Replacements***

SPECIFIC PURPOSE, PROBLEM INTENDED TO BE ADDRESSED, NECESSITY, AND ANTICIPATED BENEFIT

General Background

The Song-Beverly Consumer Warranty Act (commencing with Civ. Code, § 1790) contains provisions that provide warranty protections to purchasers of both new and used consumer goods. The act includes provisions (Civ. Code, §§ 1793.2 - 1793.26) that require compensation to California consumers of defective new motor vehicles – provisions commonly referred to as California’s “Lemon Law.” As relevant here, the Lemon Law provides that if the manufacturer or its representative is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer shall either promptly replace the new motor vehicle or promptly make restitution to the buyer. (Civ. Code, § 1793.2, subd. (d)(2).)

Under the existing Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.), a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant here, a “sale” and a “purchase.” (Rev. & Tax. Code, §§ 6006, 6010.) For a lease that is a “sale” and a “purchase,” the tax is measured by the rentals payable. However, as provided in subdivision (c)(1) of California Code of Regulations, title 18, section (Regulation) 1660, *Leases of Tangible Personal Property – In General*, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686, *Receipts for Tax Paid to Retailers*. The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

The Lemon Law originally provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other collateral charges, *sales tax*. (Civ. Code, § 1793.2.) The Lemon Law further required the State Board of Equalization (Board) to reimburse the manufacturer for an amount equal to the *sales tax* which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer when satisfactory proof was provided that:

- The retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale of that motor vehicle; and
- The manufacturer complied with Civil Code section 1793.23, subdivision (c), which pertains to inscribing the ownership certificate of a reacquired vehicle with the notation

“Lemon Law Buyback” and affixing a decal to the vehicle regarding the notation on the ownership certificate. (Civ. Code, § 1793.25.)

However, the Lemon Law was silent with respect to whether restitution was required to include *use* tax and whether the Board was required to reimburse a manufacturer for use tax paid to or for a buyer or lessee or included in restitution paid to a buyer or lessee.

Assembly Bill No. 242 (AB 242) (Stats. 2011, ch. 727, §§ 1 and 2) amended the Lemon Law, specifically Civil Code sections 1793.2 and 1793.25, to make technical corrections sponsored by the Board. The amendments clarify that restitution, under the Lemon Law, includes *use* tax paid or payable by a buyer, including a lessee, of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to the Lemon Law. And, AB 242 provides that the Board-sponsored amendments to the Lemon Law are declaratory of existing law. (AB 242, § 21.)

#### *Civil Code section 1793.2*

With respect to Civil Code section 1793.2, AB 242 specifically:

- Amended subdivision (d)(2)(B) to add “use tax” to the collateral charges which a buyer is entitled to receive in cases of restitution; and
- Added subdivision (d)(2)(D) to specify that “[p]ursuant to section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

Therefore, in the case of restitution, Civil Code section 1793.2, subdivision (d)(2)(B) and (D), currently provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer or lessee, including any collateral charges such as “sales or use tax.”

#### *Civil Code section 1793.25*

With respect to Civil Code section 1793.25 and as relevant here, AB 242 specifically:

- Amended subdivision (a) to specify the Board shall reimburse the manufacturer of a new motor vehicle for an amount equal to the sales tax “or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or includes in making restitution to the buyer “or lessee” under the Lemon Law;
- Expanded the satisfactory proof that tax was paid, under subdivision (a), to include proof that:
  - “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or
  - “The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of that motor vehicle”; and
- Added subdivision (e) which specifies that “the amount of use tax that the [Board] is required to reimburse the manufacturer shall be limited to the amount of use tax the

manufacturer is required to pay to or for the lessee pursuant to [Civil Code] section 1793.2.”

As a result, Civil Code section 1793.25, subdivision (a), currently provides, in relevant part, that the Board shall reimburse a manufacturer for an amount equal to the sales or use tax which the manufacturer pays to or for a buyer or lessee when providing a replacement vehicle, or includes in making restitution to the buyer or lessee. Also, in order to obtain reimbursement, subdivision (a) currently requires a manufacturer to provide satisfactory proof that it complied with Civil Code subdivision 1793.23, subdivision (c), which pertains to inscribing the ownership certificate of a reacquired vehicle with the notation “Lemon Law Buyback” and affixing a decal to the vehicle regarding the notation on the ownership certificate. And, subdivision (a) requires a manufacture to provide satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle has paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of that motor vehicle.

### Proposed Amendments

#### *Need for Clarification*

Subdivision (b)(2) of Regulation 1655, *Returns, Defects and Replacements*, explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement<sup>1</sup> included in restitution paid to a buyer under the Lemon Law. However, there is an issue (or problem within the meaning of Gov. Code, § 11346.2, subdivision (b)) because Regulation 1655 does not indicate that AB 242 made amendments to Civil Code sections 1793.2 and 1793.25 to make clear that restitution, under the Lemon Law, includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or includes in making restitution to a buyer or lessee, under the Lemon Law. Therefore, the Board’s Business Taxes Committee (BTC) staff determined that amendments to Regulation 1655 are needed in order to make Regulation 1655 consistent with and implement, interpret, and make specific the amendments to the Lemon Law made by AB 242 (discussed above).

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<sup>1</sup> California imposes sales tax on retailers for the privilege of selling tangible personal property at retail. (Rev. & Tax. Code, § 6051.) Although sales tax is imposed on retailers, retailers may collect sales tax reimbursement from their customers, as explained in Regulation 1700, *Reimbursement for Sales Tax*.

### *Interested Parties Process*

As a result of AB 242, BTC staff drafted amendments to Regulation 1655. Specifically, the draft amendments suggested adding language to Regulation 1655, subdivision (b)(2)(A) to incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D), by specifying that, for purposes of Regulation 1655, the term buyer includes a lessee of a new motor vehicle. The draft amendments suggested adding “or use” tax to where the current regulation refers to “sales tax or sales tax reimbursement” in subdivision (b)(2)(B) and (C). The draft amendments suggested adding “or lease” after “sales” where the current regulation refers to “sales agreement” and after “sale” where the current regulation refers to “retail sale” in subdivision (b)(2)(B). The draft amendments also suggested adding “or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer” in subdivision (b)(2)(B).

In addition, the draft amendments suggested revising and reformatting the last sentence in Regulation 1655, subdivision (b)(2)(B), which currently requires a manufacturer, when filing a claim for refund for sales tax or sales tax reimbursement included in restitution paid to a buyer, to submit evidence that the dealer who made the retail sale of the non-conforming motor vehicle to that buyer reported and paid sales tax on the gross receipts from that sale. The revised and reformatted sentence requires a manufacturer, when filing a claim for refund for sales or use tax or sales tax reimbursement included in restitution paid to a buyer, including a lessee, under the Lemon Law, to provide “evidence of one of the following” from a list that includes proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) “The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.” The draft amendments also suggested adding a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

BTC staff subsequently prepared a discussion paper regarding the amendments made to the Lemon Law by AB 242 and staff’s draft amendments to Regulation 1655, provided the discussion paper and its draft amendments to Regulation 1655 to the interested parties, and conducted an interested parties meeting on August 8, 2013, to discuss the draft amendments to Regulation 1655. During the interested parties meeting, a participant inquired as to how the provisions of Regulation 1655 would apply to a transaction in which a lessor paid tax at the time the lessor purchased a vehicle which the lessor would then lease. Staff considered the scenario and, subsequent to the meeting, staff explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement from the lessor. (See Reg. 1660, subd. (c)(2) and (3), regarding property purchased tax-paid and leased in substantially the same form as acquired.) And, staff explained that, with respect to sales tax transactions, the existing provisions of Regulation 1655 would apply to a manufacturer’s claim for a refund for sales tax reimbursement the manufacturer included in restitution paid to a lessor, under the Lemon Law. Furthermore, staff noted that AB 242 did not change the application of the Lemon Law to sales

tax transactions, and that questions regarding the application of Regulation 1655 to sales tax transactions were beyond the scope of the current interested parties process, which was to discuss the issue of whether to amend Regulation 1655 to clarify the new provisions of the Lemon Law applicable to use tax transactions.

Since BTC staff did not receive any other inquiries or comments regarding the draft amendments during or subsequent to the first interested parties meeting and staff had no changes to its recommendation to amend Regulation 1655, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff's draft amendments. Staff also notified interested parties that comments could be submitted up to October 17, 2013, for consideration in the preparation of a Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

#### *December 17, 2013 BTC Meeting*

Subsequently, staff prepared Formal Issue Paper 13-012 and distributed it to the Board Members for consideration at the Board's December 17, 2013, BTC meeting. Formal Issue Paper 13-012 recommended that the Board approve and authorize publication of the amendments to Regulation 1655 (discussed above) in order to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).<sup>2</sup>

During the December 17, 2013, BTC meeting, the Board Members unanimously voted to propose the amendments to Regulation 1655 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1655 are reasonably necessary for the specific purpose of making the regulation consistent with and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242, and addressing the issue (or problem) that Regulation 1655 does not currently indicate that AB 242 made amendments to Civil Code sections 1793.2 and 1793.25.

The Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing

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<sup>2</sup> The formal issue paper also recommended that the Board approve a minor grammatical change capitalizing the first letter in the word "Board" in Regulation 1655, subdivision (b)(2)(B).

additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The adoption of the proposed amendments to Regulation 1655 is not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to Regulation 1655 or the proposed amendments to Regulation 1655.

#### DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 13-012, the exhibits to the issue paper, and the comments made during the Board's discussion of the issue paper during its December 16, 2013, BTC meeting in deciding to propose the amendments to Regulation 1655 described above.

#### ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulation 1655 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 to Regulation 1655 at this time because the Board determined that the proposed amendments are reasonably necessary for the reasons set forth above.

The Board did not reject any reasonable alternative to the proposed amendments to Regulation 1655 that would lessen any adverse impact the proposed action may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed action. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

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

Prior to the enactment of AB 242, the Lemon Law expressly provided that a manufacturer was required to make restitution to a buyer in an amount equal to the actual price paid or payable by the buyer, including *sales* tax. The Lemon Law further required the Board to reimburse a manufacturer for an amount equal to the *sales* tax which the manufacturer paid to or for a buyer when providing a replacement vehicle or making restitution. However, the Lemon Law did not expressly address the treatment of *use* tax.

As previously explained in more detail above, AB 242 made specific amendments to Civil Code sections 1793.2 and 1793.25. The amendments clarify that restitution, under the Lemon Law, includes *use* tax paid or payable by a buyer, including a lessee, of a new motor vehicle. The amendments also clarify that the Board is required to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California's "Lemon Law." In addition, in order to claim reimbursement for such use tax, the amendments specifically require a manufacturer to provide satisfactory evidence that the buyer paid use tax on the sales price of or the lessee paid use tax on the rentals payable from the lease of the vehicle that the manufacturer replaced or made restitution for. And, the amendments specifically provide that, with regard to leases, the amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee under the Lemon Law.

As previously explained in more detail above, subdivision (b)(2) of Regulation 1655 explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. However, Regulation 1655 does not indicate that AB 242 made amendments to the Lemon Law to clarify that restitution includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution.

Also, as previously explained above, the proposed amendments to Regulation 1655 incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle.
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund.
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee.

As a result, the proposed amendments make Regulation 1655 consistent with the amendments made to the Lemon Law by AB 242, the proposed amendments do not mandate that individuals or businesses do anything that is not already required by the Lemon Law, and there is nothing in the proposed amendments that would significantly change how individuals and businesses would generally behave, in the absence of the proposed regulatory action, or that would impact revenue. Therefore, the Board estimates that the proposed amendments will not have a measurable economic impact on individuals and business that is in addition to whatever economic impact the amendments made to the Lemon Law by AB 242 have had and will have on individuals and businesses. The Board has determined that the proposed amendments to Regulation 1655 are not

a major regulation, as defined in Government Code section 11342.548 and California Code of Regulations, title 1, section 2000, because the Board has estimated that the proposed amendments will not have an economic impact on California business enterprises and individuals in an amount exceeding fifty million dollars (\$50,000,000) during any 12-month period. And, the Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

In addition, based on these facts and all of the information in the rulemaking file, the Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 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 1655 will not affect the benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulation 1655 will not have a significant adverse economic impact on business.

The proposed amendments to Regulation 1655 may affect small businesses.

**Text of Proposed Amendments to  
California Code of Regulations, Title 18, Section 1655**

**1655. Returns, Defects and Replacements.**

**(a) Returned Merchandise.**

(1) **In General.** Except as provided in paragraph (2) of this subdivision, the amount upon which tax is computed does not include the amount charged for merchandise returned by customers if, (1) the full sale price, including that portion designated as “sales tax,” is refunded either in cash or credit, and (2) the customer, in order to obtain the refund or credit, is not required to purchase other property at a price greater than the amount charged for the property that is returned. Refund or credit of the entire amount is deemed to be given when the purchase price, less rehandling and restocking costs, is refunded or credited to the customer. The amount withheld for rehandling and restocking may not exceed the actual cost of rehandling and restocking the returned merchandise. However, in lieu of using the actual cost for each transaction, the amount withheld for rehandling and restocking may be a percentage of the sales price determined by the average cost of rehandling and restocking returned merchandise during the previous accounting cycle (generally one year). If the seller elects to withhold rehandling and restocking amounts based on a percentage of sales price, the seller is bound by that election for the entire accounting cycle for which the election is made and must apply that percentage in lieu of actual cost during that period on all returned merchandise transactions for which rehandling and restocking costs are withheld. The amount withheld as rehandling and restocking costs may not include compensation for increased overhead costs because of the return, for refinishing or restoring the property to salable condition where the necessity therefore is occasioned by customer usage, or for any expense prior to the “sale” (i.e., transfer of title, lease, or possession under a conditional sale contract). Sellers must maintain adequate records which may be verified by audit, documenting the percentage used.

**(2) Contract Cancellation Options Required by Car Buyer’s Bill of Rights.**

**(A) Contract Cancellation Option.** On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include the purchase price for a contract cancellation option agreement with respect to a contract to purchase a used vehicle with a purchase price of less than forty thousand dollars (\$40,000), which a dealer is required to offer to a buyer pursuant to Vehicle Code section 11713.21. The purchase price for a contract cancellation option described in this subparagraph shall not exceed:

1. Seventy-five dollars (\$75) for a vehicle with a cash price of five thousand dollars (\$5,000) or less;
2. One hundred fifty dollars (\$150) for a vehicle with a cash price of more than five thousand dollars (\$5,000), but not more than ten thousand dollars (\$10,000);
3. Two hundred fifty dollars (\$250) for a vehicle with a cash price of more than ten thousand dollars (\$10,000), but not more than thirty thousand dollars (\$30,000); or

4. One percent of the purchase price for a vehicle with a cash price of more than thirty thousand dollars (\$30,000), but less than forty thousand dollars (\$40,000).

(B) Restocking Fee. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include the dollar amount of a restocking fee the buyer must pay to the dealer to exercise the right to cancel a purchase of a used car under a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph. The dollar amount of a restocking fee described in this subparagraph shall not exceed:

1. One hundred seventy-five dollars (\$175) if the vehicle’s cash price is five thousand dollars (\$5,000) or less;
2. Three hundred fifty dollars (\$350) if the vehicle’s cash price is more than five thousand dollars (\$5,000), but less than ten thousand dollars (\$10,000); or
3. Five hundred dollars (\$500) if the vehicle’s cash price is ten thousand dollars (\$10,000) or more.

(C) Amounts Refunded to Customers. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include that portion of the selling price for a used motor vehicle that is refunded to the buyer due to the buyer’s exercise of the right to return the vehicle for a refund, which is contained in a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph.

(b) Defective Merchandise.

(1) In General. Amounts credited or refunded by sellers to consumers on account of defects in merchandise sold may be excluded from the amount on which tax is computed. If, however, defective merchandise is accepted as part payment for other merchandise and an additional allowance or credit is given on account of its defective condition, only the amount allowed or credited on account of defects may be excluded from taxable gross receipts. The amount allowed as the “trade-in” value must be included in the measure of tax.

(2) Restitution or Replacement Under California Lemon Law.

(A) General. Under subdivision (d) of Civil Code section 1793.2, if a manufacturer is unable to service or repair a “new motor vehicle,” as that term is defined in subdivision (e)(2) of Civil Code section 1793.22, to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer must either replace the motor vehicle or provide the buyer restitution of the purchase price, less specified amounts, at the buyer’s election.

For purposes of this regulation, the term buyer shall include a lessee of a new motor vehicle.

(B) Restitution. A manufacturer who pays a buyer restitution pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 is entitled to a refund of the amount of sales or use tax, or sales tax reimbursement included in the restitution paid by the manufacturer to the buyer. The manufacturer may file a claim for refund of that amount with the Board. The claim must include a statement that the claim is submitted in accordance with the provisions of section 1793.25 of the Civil Code. The manufacturer must submit with the claim documents evidencing that restitution was made pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 including: a copy of the original sales or lease agreement between the buyer and the dealer or lessor of the non-conforming motor vehicle; copies of documents showing all deductions made in calculating the amount of restitution paid to the buyer along with full explanations for those deductions, including settlement documents and odometer statements; a copy of the title branded “Lemon Law Buyback” for the non-conforming motor vehicle returned by the buyer; and proof that the decal the manufacturer is required to affix to that motor vehicle has been so affixed in accordance with section 11713.12 of the Vehicle Code. The manufacturer must also submit with the claim the seller’s permit number of the dealer or lessor who made the retail sale or lease of the non-conforming motor vehicle to the buyer, and evidence for one of the following:

1. that the dealer had reported and paid sales tax on the gross receipts from that sale; or

2. The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state; or

3. The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer restitution is not relevant for purposes of determining whether restitution has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(C) Replacement. For purposes of this regulation, a manufacturer who, pursuant to subdivision (d)(2) of Civil Code section 1793.2, replaces a non-conforming motor vehicle with a new motor vehicle substantially identical to the motor vehicle replaced is replacing the motor vehicle under the terms of the mandatory warranty. No additional tax is due unless the buyer is required to pay an additional amount to receive the replacement motor vehicle, in which case tax is due measured by the amount of that payment. If an amount is refunded to the customer as part of the exchange of the non-conforming motor vehicle for the replacement motor vehicle, then that amount is regarded as restitution for purposes of this regulation if it satisfies the requirements of subdivision (d)(2) of Civil Code section 1793.2. The manufacturer may file a claim for refund under subdivision (b)(2)(B) of this regulation for the amount of sales or use tax, or sales tax reimbursement that is included in the amount of that restitution paid by the manufacturer to the buyer.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer a replacement is not relevant for purposes of determining whether the replacement has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(D) The amount of use tax the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee pursuant to Civil Code section 1793.2.

(c) Replacement Parts - Warranties.

(1) In General -Definitions. "Mandatory Warranty." A warranty is mandatory within the meaning of this regulation when the buyer, as a condition of the sale, is required to purchase the warranty or guaranty contract from the seller. "Optional Warranty." A warranty is optional within the meaning of this regulation when the buyer is not required to purchase the warranty or guaranty contract from the seller, i.e., the buyer is free to contract with anyone he or she chooses.

(2) Mandatory Warranties. The sale of tangible personal property includes the furnishing, pursuant to the guaranty provisions of the contract of sale, or mandatory warranty, of replacement parts or materials, and if the property subject to the warranty is sold at retail, the measure of the tax includes any amount charged for the guaranty or warranty, whether or not separately stated. The sale of the replacement parts and materials to the seller furnishing them thereunder is a sale for resale and not taxable.

(3) Optional Warranties. The person obligated under an optional warranty contract to furnish parts, materials, and labor necessary to maintain the property is the consumer of the materials and parts furnished and tax applies to the sale of such items to that person. If he or she purchased the property for resale or from outside California, without tax paid on the purchase price, he or she must report and pay tax upon the cost of such property to him or her when he or she appropriates it to the fulfillment of the contract of warranty.

(4) Deductibles. A deductible paid by a customer under the terms of a mandatory or optional warranty contract is subject to tax measured by the amount of the deductible allocable to the sale of tangible personal property to the customer. For example, if the itemized sales price of tangible personal property (or the fair retail value if not separately itemized) provided pursuant to a warranty is 50 percent of the total fair retail value of the repairs and the deductible is \$100, 50 percent of that deductible, \$50, would be allocable to the sale of tangible personal property and would be subject to tax, whether the warranty were optional or mandatory. Unless otherwise stated in the warranty contract, when either an optional or a mandatory warranty provides that the customer will pay a deductible towards repairs and services provided under the warranty, the person providing the warranty contract is liable for any tax or tax reimbursement otherwise payable by the customer with respect to that deductible.

**Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6006-6012 and 6012.3, Revenue and Taxation Code; Sections 1793.2-1793.25, Civil Code; and Sections 11713.12 and 11713.21, Vehicle Code.**

## Regulation History

**Type of Regulation:** Sales and Use Tax

Regulation: 1655

Title: 1655, *Returns, Defects and Replacements*

**Preparation:** Monica Silva

**Legal Contact:** Monica Silva

The proposed amendments to Regulation 1655, *Returns, Defects and Replacements*, clarify that the regulation's provisions regarding restitution and replacement under the "Lemon Law" apply to use tax under specified circumstances.

### History of Proposed Regulation:

April 22-24, 2014	Public Hearing
February 14, 2014	OAL publication date; 45-day public comment period begins; Interested Parties mailing
February 4, 2014	Notice to OAL
December 17, 2013	Business Tax Committee, Board Authorized Publication (Vote 5-0)

Sponsor: NA

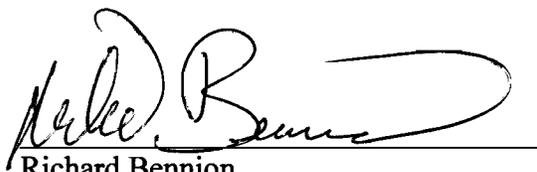
Support: NA

Oppose: NA

## Statement of Compliance

The State Board of Equalization, in process of adopting Sales and Use Taxes Regulation 1655, *Returns, Defects and Replacements*, did comply with the provision of Government Code section 11346.4(a)(1) through (4). A notice to interested parties was mailed on February 14, 2014, 67 days prior to the public hearing.

April 21, 2014

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

APRIL 22, 2014

ITEM F

PUBLIC HEARINGS

ITEM F2

PROPOSED ADOPTION OF AMENDMENTS TO SALES AND USE TAX  
REGULATION 1655, RETURNS, DEFECTS AND REPLACEMENTS

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 Staff:

Monica Silva  
Tax Counsel III  
Legal Department

Bradley Heller  
Tax Counsel IV  
Legal Department

---oOo---

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

4 ---oOo---

5 MR. HORTON: Ms. Richmond.

6 MS. RICHMOND: Our next item is F2,  
7 Proposed Adoption of Amendments to Sales and Use Tax  
8 Regulation 1655, Returns, Defects and Replacements.

9 MS. SILVA: Monica Silva with the Legal  
10 Department. With me is Mr. Bradley Heller.

11 We request that the Board vote to adopt  
12 amendments to Regulation 1655. We've received no  
13 public comments regarding the proposed amendments.

14 MR. HORTON: Thank you very much.

15 Discussion, Members?

16 Hearing none, is there a motion?

17 MS. YEE: So move.

18 MR. HORTON: Moved by Member Steel to adopt  
19 staff recommendation. Second by Member Yee.

20 Without objection, Members, such will be  
21 the order.

22 Thank you very much.

23 ---oOo---

REPORTER'S CERTIFICATE

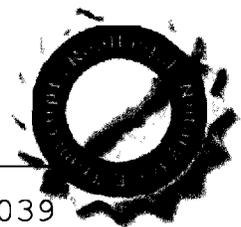
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State of California )  
 ) ss  
County of Sacramento )

I, KATHLEEN SKIDGEL, Hearing Reporter for the California State Board of Equalization certify that on April 22, 2014 I recorded verbatim, in shorthand, to the best of my ability, the proceedings in the above-entitled hearing; that I transcribed the shorthand writing into typewriting; and that the preceding pages 1 through 3 constitute a complete and accurate transcription of the shorthand writing.

Dated: April 23, 2014

*Kathleen Skidgel*



KATHLEEN SKIDGEL, CSR #9039

Hearing Reporter

**2014 MINUTES OF THE STATE BOARD OF EQUALIZATION**

Tuesday, April 22, 2014

**PUBLIC HEARINGS****F1 Property Taxes - State Assesseees' Presentations on the Valuation of State-Assessed Properties**

Ken Thompson, Chief, State-Assessed Properties Division, Property and Special Taxes Department, was available to answer question regarding presentations on the valuation of state-assessed properties.

Speaker: Peter W. Michaels, Law Offices of Peter Michaels representing State Assessed Gas/Electric, Intercounty Pipeline, Telephone and Railroad Companies

**F2 Proposed Adoption of Amendments to Sales and Use Tax Regulation 1655, Returns, Defects and Replacements**

Monica Silva, Tax Counsel, Tax and Fee Programs Division, Legal Department, made introductory remarks regarding the proposed amendments, which clarify the regulation's provisions regarding restitution and replacement under the "Lemon Law" apply to use tax under specified circumstances (Exhibit 4.7).

Speakers were invited to address the Board, but there were none.

Action: Upon motion of Ms. Steel, seconded by Ms. Yee and unanimously carried, Mr. Horton, Ms. Steel, Ms. Yee, Mr. Runner and Ms. Mandel voting yes, the Board adopted the proposed amendments as recommended by staff.

**F3 Proposed Adoption of Amendments to Special Taxes and Fees Regulation 4902, Relief from Liability**

Pamela Mash, Tax Counsel, Tax and Fee Programs Division, Legal Department, made introductory remarks regarding the proposed amendments, which extend relief to a person who relies on advice provided in a prior audit of a related person, under specific circumstances (Exhibit 4.8).

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**

The Board deferred consideration of the following matter: *G1.1 Ronald Avedisian, 434518 (AC)*.

**Note: These minutes are not final until Board approved.**



STATE OF CALIFORNIA

**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

CYNTHIA BRIDGES  
Executive Director

**February 14, 2014**

**To Interested Parties:**

**Notice of Proposed Regulatory Action**

**The State Board of Equalization Proposes to Adopt Amendments to  
California Code of Regulations, Title 18,  
Section 1655, *Returns, Defects and Replacements***

**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) 1655, *Returns, Defects and Replacements*, which incorporate and implement, interpret, and make specific amendments made to Civil Code sections 1793.2 and 1793.25, by Assembly Bill No. 242 (AB 242) (Stats. 2011, ch. 727). The amendments to these sections require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California's "Lemon Law."

The proposed amendments to Regulation 1655, subdivision (b)(2)(A) incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D) by specifying that the term buyer includes a lessee of a new motor vehicle. The proposed amendments to Regulation 1655, subdivisions (b)(2)(B) and (C) add "or use" tax where the current regulation refers to "sales tax or sales tax reimbursement." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add "or lease" after "sales" where the current regulation refers to "sales agreement" and after "sale" where the current regulation refers to "retail sale." The proposed amendments to Regulation 1655, subdivision (b)(2)(B) add "or lessor" after "dealer" where the current regulation refers to "the buyer and the dealer" and "the seller's permit number of the dealer." The proposed amendments revise and reformat the last sentence in Regulation 1655, subdivision (b)(2)(B) to require a manufacturer, when filing a claim for refund, to include "evidence of one of the following" from a list of proof that: (1) "The dealer had reported and paid sales tax on the

gross receipts from that sale”; (2) ”The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) “The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The proposed amendments also add a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

## **PUBLIC HEARING**

The Board will conduct a meeting in Room 121, at 450 N Street, Sacramento, California, on April 22-24, 2014. The Board will provide notice of the meeting to any person who requests that notice in writing and make the notice, including the specific agenda for the meeting, available on the Board’s Website at [www.boe.ca.gov](http://www.boe.ca.gov) at least 10 days in advance of the meeting.

A public hearing regarding the proposed regulatory action will be held at 10:00 a.m. or as soon thereafter as the matter may be heard on April 22, 2014. At the hearing, any interested person may present or submit oral or written statements, arguments, or contentions regarding the adoption of the proposed amendments to Regulation 1655.

## **AUTHORITY**

RTC section 7051

## **REFERENCE**

RTC sections 6006-6012, and 6012.3; Civil Code sections 1793.2-1793.25; Vehicle Code sections 11713.12 and 11713.21

## **INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW**

### Current Law

#### *General*

The Song-Beverly Consumer Warranty Act (commencing with Civ. Code, § 1790) contains provisions that provide warranty protections to purchasers of both new and used consumer goods. The act includes provisions (Civ. Code §§ 1793.2 - 1793.26) that require compensation to California consumers of defective new motor vehicles – provisions commonly referred to as California’s “Lemon Law.” The Lemon Law provides, in relevant part, that if a manufacturer or its representative in this state, such as an authorized dealer, is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer is required to either promptly replace the vehicle or make restitution to the buyer. (Civ. Code, § 1793.2, subd. (d)(2).)

Under the existing Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.), a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant here, a “sale” and a “purchase.” (Rev. & Tax. Code, §§ 6006, 6010.) For a lease that is a “sale” and a “purchase,” the tax is measured by the rentals payable. However, as provided in subdivision (c)(1) of Regulation 1660, *Leases of Tangible Personal Property – In General*, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686, *Receipts for Tax Paid to Retailers*. The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

The Lemon Law originally provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other collateral charges, *sales tax*. (Civ. Code, § 1793.2.) The Lemon Law further required the Board to reimburse the manufacturer for an amount equal to the *sales tax* which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer when satisfactory proof was provided that the retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale, and that the manufacturer had complied with the requirements of Civil Code section 1793.23, subdivision (c). However, the Lemon Law was silent with respect to whether restitution was required to include *use tax* and whether the Board was required to reimburse a manufacturer for use tax paid to or for a buyer or lessee or included in restitution paid to a buyer or lessee.

As relevant here, AB 242 amended the Lemon Law, specifically Civil Code sections 1793.2 and 1793.25, to make technical corrections sponsored by the Board. The amendments clarify that restitution, under the Lemon Law, includes *use tax* paid or payable by a buyer, including a lessee, of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use tax* that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to the Lemon Law. And, AB 242 provides that the Board-sponsored amendments to the Lemon Law are declaratory of existing law. (AB 242, § 21.)

In the case of restitution, Civil Code section 1793.2, subdivision (d)(2)(B) now provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer, including any collateral charges “such as sales or use tax.” And, Civil Code section 1793.2, subdivision (d)(2)(D) now specifies that “Pursuant to Section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

With respect to reimbursement, Civil Code section 1793.25, subdivision (a) now expressly requires the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to “the sales tax or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or includes in making restitution to the buyer “or lessee” under the Lemon Law, and, as a condition to receiving reimbursement, requires a manufacturer to provide satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of that motor vehicle.

Also, Civil Code section 1793.25, subdivision (e) now provides that “The amount of use tax that the State Board of Equalization is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee” under the Lemon Law.

### Effect, Objective, and Benefits of the Proposed Amendments to Regulation 1655

#### *Need for Clarification*

Subdivision (b)(2) of Regulation 1655 explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. However, Regulation 1655 does not indicate that AB 242 clarified that, under the Lemon Law, restitution includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle and required the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or includes in making restitution to a buyer or lessee, under the Lemon Law. Therefore, the Board’s Business Taxes Committee (BTC) staff determined that amendments to Regulation 1655 are needed in order to make the regulation consistent with and implement, interpret, and make specific AB 242’s amendments to the Lemon Law set forth above.

#### *Interested Parties Process*

As a result of AB 242, BTC staff drafted amendments to Regulation 1655. Specifically, the draft amendments suggested adding language to Regulation 1655, subdivision (b)(2)(A) to incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D), by specifying that, for purposes of Regulation 1655, the term buyer includes a lessee of a new motor vehicle. The draft amendments suggested adding “or use” tax to where the current regulation refers to “sales tax or sales tax reimbursement” in subdivision (b)(2)(B) and (C). The draft amendments suggested adding “or lease” after “sales” where the current regulation refers to “sales agreement” and after “sale” where the current regulation refers to “retail sale” in subdivision (b)(2)(B). The draft amendments also suggested adding “or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer” in subdivision (b)(2)(B).

In addition, the draft amendments suggested revising and reformatting the last sentence in Regulation 1655, subdivision (b)(2)(B), which currently requires a manufacturer, when filing a claim for refund for sales tax or sales tax reimbursement included in restitution paid to a buyer,

to submit evidence that the dealer who made the retail sale of the non-conforming vehicle to that buyer reported and paid sales tax on the gross receipts from that sale. The revised and reformatted sentence requires a manufacturer, when filing a claim for refund for sales or use tax or sales tax reimbursement included in restitution paid to a buyer, including a lessee, under the Lemon Law, to provide “evidence of one of the following” from a list that includes proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of the vehicle.” The draft amendments also suggested adding a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

BTC staff subsequently prepared a discussion paper regarding the amendments made to the Lemon Law by AB 242 and staff’s draft amendments to Regulation 1655, provided the discussion paper and its draft amendments to Regulation 1655 to the interested parties, and conducted an interested parties meeting on August 8, 2013, to discuss the draft amendments to Regulation 1655. During the interested parties meeting, a participant inquired as to how the provisions of Regulation 1655 would apply to a transaction in which a lessor paid tax at the time the lessor purchased a vehicle which the lessor would then lease. Staff considered the scenario and, subsequent to the meeting, staff explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement from the lessor. (See Reg. 1660, subd. (c)(2) and (3), regarding property purchased tax-paid and leased in substantially the same form as acquired.) And, staff explained that, with respect to sales tax transactions, the existing provisions of Regulation 1655 would apply to a manufacturer’s claim for a refund for sales tax reimbursement the manufacturer included in restitution paid to a lessor, under the Lemon Law. Furthermore, staff noted that AB 242 did not change the application of the Lemon Law to sales tax transactions, and that questions regarding the application of Regulation 1655 to sales tax transactions were beyond the scope of the current interested parties process, which was to discuss the issue of whether to amend Regulation 1655 to clarify the new provisions of the Lemon Law applicable to use tax transactions.

Since BTC staff did not receive any other inquiries or comments regarding its draft amendments during or subsequent to the first interested parties meeting and staff had no changes to its recommendation to amend Regulation 1655, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff’s draft amendments. Staff also notified interested parties that comments could be submitted up to October 17, 2013, for consideration in the preparation of a Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

*December 17, 2013, BTC Meeting*

Subsequently, staff prepared Formal Issue Paper 13-012 and distributed it to the Board Members for consideration at the Board's December 17, 2013, BTC meeting. Formal Issue Paper 13-012 recommended that the Board approve and authorize publication of the amendments to Regulation 1655 (discussed above) in order to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).

During the December 17, 2013, BTC meeting, the Board Members unanimously voted to propose the amendments to Regulation 1655 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1655 are reasonably necessary to have the effect and accomplish the objective of making the regulation consistent with and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The Board has performed an evaluation of whether the proposed amendments to Regulation 1655 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 1655 is the only state regulation prescribing the requirements for the Board to reimburse a manufacturer under Civil Code section 1793.25. In addition, the Board has determined that there are no comparable federal regulations or statutes to Regulation 1655 or the proposed amendments to Regulation 1655.

**NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS**

The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will result in no direct or indirect cost or savings to any state agency, cost to any local agencies or school districts that is required to be reimbursed under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code, other non-discretionary cost or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

**NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS**

The Board has made an initial determination that the adoption of the proposed amendments to Regulation 1655 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 1655 may affect small business.

**NO COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES**

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

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

The Board has prepared the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. The Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 will not affect the benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

**NO SIGNIFICANT EFFECT ON HOUSING COSTS**

The adoption of the proposed amendments to Regulation 1655 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 Monica Gonzalez Silva, Tax Counsel III, by telephone at (916) 323-3138, by e-mail at [Monica.Silva@boe.ca.gov](mailto:Monica.Silva@boe.ca.gov), or by mail at State Board of Equalization, Attn: Monica Gonzalez Silva, 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](mailto:Richard.Bennion@boe.ca.gov), or by mail at State Board of Equalization, Attn: Rick Bennion, MIC:80, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0080.

## **WRITTEN COMMENT PERIOD**

The written comment period ends at 10:00 a.m. on April 22, 2014, or as soon thereafter as the Board begins the public hearing regarding the adoption of the proposed amendments to Regulation 1655 during the April 22-24, 2014, Board meeting. Written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, will be presented to the Board and the Board will consider the statements, arguments, and/or contentions contained in those written comments before the Board decides whether to adopt the proposed amendments to Regulation 1655. 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 1655 illustrating the express terms of the proposed amendments. The Board has also prepared an initial statement of reasons for the adoption of the proposed amendments to Regulation 1655, which includes the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed

amendments and the initial statement of reasons are also available on the Board's Website at [www.boe.ca.gov](http://www.boe.ca.gov).

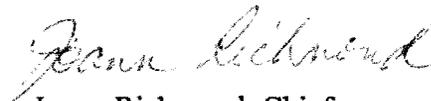
**SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8**

The Board may adopt the proposed amendments to Regulation 1655 with changes that are nonsubstantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the Board will make the full text of the proposed regulation, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting regulation will be mailed to those interested parties who commented on the original proposed regulation orally or in writing or who asked to be informed of such changes. The text of the resulting regulation will also be available to the public from Mr. Bennion. The Board will consider written comments on the resulting regulation that are received prior to adoption.

**AVAILABILITY OF FINAL STATEMENT OF REASONS**

If the Board adopts the proposed amendments to Regulation 1655, 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](http://www.boe.ca.gov)

Sincerely,

  
Joann Richmond, Chief  
Board Proceedings Division

JR:reb

**Initial Statement of Reasons for  
Proposed Amendments to California Code of Regulations,  
Title 18, Section 1655, *Returns, Defects and Replacements***

SPECIFIC PURPOSE, PROBLEM INTENDED TO BE ADDRESSED, NECESSITY, AND ANTICIPATED BENEFIT

General Background

The Song-Beverly Consumer Warranty Act (commencing with Civ. Code, § 1790) contains provisions that provide warranty protections to purchasers of both new and used consumer goods. The act includes provisions (Civ. Code, §§ 1793.2 - 1793.26) that require compensation to California consumers of defective new motor vehicles – provisions commonly referred to as California’s “Lemon Law.” As relevant here, the Lemon Law provides that if the manufacturer or its representative is unable to service or repair a new motor vehicle to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer shall either promptly replace the new motor vehicle or promptly make restitution to the buyer. (Civ. Code, § 1793.2, subd. (d)(2).)

Under the existing Sales and Use Tax Law (Rev. & Tax. Code, § 6001 et seq.), a lease of tangible personal property, including a lease of a motor vehicle, is, with exceptions not relevant here, a “sale” and a “purchase.” (Rev. & Tax. Code, §§ 6006, 6010.) For a lease that is a “sale” and a “purchase,” the tax is measured by the rentals payable. However, as provided in subdivision (c)(1) of California Code of Regulations, title 18, section (Regulation) 1660, *Leases of Tangible Personal Property – In General*, the applicable tax is generally use tax, not sales tax, and the lessor is required to collect the use tax from the lessee at the time the amount of rent is paid and give him or her a receipt as prescribed in Regulation 1686, *Receipts for Tax Paid to Retailers*. The lessee is not relieved from liability for the tax until he or she is given such a receipt or the tax is paid to the state.

The Lemon Law originally provided that in the case of restitution, a manufacturer was required to make restitution in an amount equal to the actual price paid or payable by the buyer, including, among other collateral charges, *sales tax*. (Civ. Code, § 1793.2.) The Lemon Law further required the State Board of Equalization (Board) to reimburse the manufacturer for an amount equal to the *sales tax* which the manufacturer paid to or for a buyer when providing a replacement vehicle or included in making restitution to the buyer when satisfactory proof was provided that:

- The retailer of the motor vehicle for which the manufacturer was making restitution had reported and paid the sales tax on the gross receipts from the sale of that motor vehicle; and
- The manufacturer complied with Civil Code section 1793.23, subdivision (c), which pertains to inscribing the ownership certificate of a reacquired vehicle with the notation

“Lemon Law Buyback” and affixing a decal to the vehicle regarding the notation on the ownership certificate. (Civ. Code, § 1793.25.)

However, the Lemon Law was silent with respect to whether restitution was required to include *use tax* and whether the Board was required to reimburse a manufacturer for use tax paid to or for a buyer or lessee or included in restitution paid to a buyer or lessee.

Assembly Bill No. 242 (AB 242) (Stats. 2011, ch. 727, §§ 1 and 2) amended the Lemon Law, specifically Civil Code sections 1793.2 and 1793.25, to make technical corrections sponsored by the Board. The amendments clarify that restitution, under the Lemon Law, includes *use tax* paid or payable by a buyer, including a lessee, of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use tax* that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to the Lemon Law. And, AB 242 provides that the Board-sponsored amendments to the Lemon Law are declaratory of existing law. (AB 242, § 21.)

#### *Civil Code section 1793.2*

With respect to Civil Code section 1793.2, AB 242 specifically:

- Amended subdivision (d)(2)(B) to add “use tax” to the collateral charges which a buyer is entitled to receive in cases of restitution; and
- Added subdivision (d)(2)(D) to specify that “[p]ursuant to section 1795.4, a buyer of a new motor vehicle shall also include a lessee of a new motor vehicle.”

Therefore, in the case of restitution, Civil Code section 1793.2, subdivision (d)(2)(B) and (D), currently provides, in relevant part, that the manufacturer shall make restitution in an amount equal to the actual price paid or payable by the buyer or lessee, including any collateral charges such as “sales or use tax.”

#### *Civil Code section 1793.25*

With respect to Civil Code section 1793.25 and as relevant here, AB 242 specifically:

- Amended subdivision (a) to specify the Board shall reimburse the manufacturer of a new motor vehicle for an amount equal to the sales tax “or use tax” which the manufacturer pays to or for the buyer “or lessee” when providing a replacement vehicle or includes in making restitution to the buyer “or lessee” under the Lemon Law;
- Expanded the satisfactory proof that tax was paid, under subdivision (a), to include proof that:
  - “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or
  - “The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of that motor vehicle”; and
- Added subdivision (e) which specifies that “the amount of use tax that the [Board] is required to reimburse the manufacturer shall be limited to the amount of use tax the

manufacturer is required to pay to or for the lessee pursuant to [Civil Code] section 1793.2.”

As a result, Civil Code section 1793.25, subdivision (a), currently provides, in relevant part, that the Board shall reimburse a manufacturer for an amount equal to the sales or use tax which the manufacturer pays to or for a buyer or lessee when providing a replacement vehicle, or includes in making restitution to the buyer or lessee. Also, in order to obtain reimbursement, subdivision (a) currently requires a manufacturer to provide satisfactory proof that it complied with Civil Code subdivision 1793.23, subdivision (c), which pertains to inscribing the ownership certificate of a reacquired vehicle with the notation “Lemon Law Buyback” and affixing a decal to the vehicle regarding the notation on the ownership certificate. And, subdivision (a) requires a manufacture to provide satisfactory proof for one of the following:

- The retailer of the motor vehicle for which the manufacturer is making restitution has reported and paid the sales tax on the gross receipts from the sale of that motor vehicle.
- The buyer of the motor vehicle has paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state.
- The lessee of the motor vehicle has paid the use tax on the rentals payable from the lease of that motor vehicle.

#### Proposed Amendments

##### *Need for Clarification*

Subdivision (b)(2) of Regulation 1655, *Returns, Defects and Replacements*, explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement<sup>1</sup> included in restitution paid to a buyer under the Lemon Law. However, there is an issue (or problem within the meaning of Gov. Code, § 11346.2, subdivision (b)) because Regulation 1655 does not indicate that AB 242 made amendments to Civil Code sections 1793.2 and 1793.25 to make clear that restitution, under the Lemon Law, includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle, and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or includes in making restitution to a buyer or lessee, under the Lemon Law. Therefore, the Board’s Business Taxes Committee (BTC) staff determined that amendments to Regulation 1655 are needed in order to make Regulation 1655 consistent with and implement, interpret, and make specific the amendments to the Lemon Law made by AB 242 (discussed above).

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<sup>1</sup> California imposes sales tax on retailers for the privilege of selling tangible personal property at retail. (Rev. & Tax. Code, § 6051.) Although sales tax is imposed on retailers, retailers may collect sales tax reimbursement from their customers, as explained in Regulation 1700, *Reimbursement for Sales Tax*.

### *Interested Parties Process*

As a result of AB 242, BTC staff drafted amendments to Regulation 1655. Specifically, the draft amendments suggested adding language to Regulation 1655, subdivision (b)(2)(A) to incorporate the new provisions of Civil Code section 1793.2, subdivision (d)(2)(D), by specifying that, for purposes of Regulation 1655, the term buyer includes a lessee of a new motor vehicle. The draft amendments suggested adding “or use” tax to where the current regulation refers to “sales tax or sales tax reimbursement” in subdivision (b)(2)(B) and (C). The draft amendments suggested adding “or lease” after “sales” where the current regulation refers to “sales agreement” and after “sale” where the current regulation refers to “retail sale” in subdivision (b)(2)(B). The draft amendments also suggested adding “or lessor” after “dealer” where the current regulation refers to “the buyer and the dealer” and “the seller’s permit number of the dealer” in subdivision (b)(2)(B).

In addition, the draft amendments suggested revising and reformatting the last sentence in Regulation 1655, subdivision (b)(2)(B), which currently requires a manufacturer, when filing a claim for refund for sales tax or sales tax reimbursement included in restitution paid to a buyer, to submit evidence that the dealer who made the retail sale of the non-conforming motor vehicle to that buyer reported and paid sales tax on the gross receipts from that sale. The revised and reformatted sentence requires a manufacturer, when filing a claim for refund for sales or use tax or sales tax reimbursement included in restitution paid to a buyer, including a lessee, under the Lemon Law, to provide “evidence of one of the following” from a list that includes proof that: (1) “The dealer had reported and paid sales tax on the gross receipts from that sale”; (2) “The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state”; or (3) “The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.” The draft amendments also suggested adding a new subdivision (b)(2)(D) to Regulation 1655 to specify that “The amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee,” as provided by Civil Code section 1793.25, subdivision (e).

BTC staff subsequently prepared a discussion paper regarding the amendments made to the Lemon Law by AB 242 and staff’s draft amendments to Regulation 1655, provided the discussion paper and its draft amendments to Regulation 1655 to the interested parties, and conducted an interested parties meeting on August 8, 2013, to discuss the draft amendments to Regulation 1655. During the interested parties meeting, a participant inquired as to how the provisions of Regulation 1655 would apply to a transaction in which a lessor paid tax at the time the lessor purchased a vehicle which the lessor would then lease. Staff considered the scenario and, subsequent to the meeting, staff explained to the participant that in the event a lessor purchases a vehicle in this state tax paid, the transaction would generally be subject to sales tax and the dealer would likely collect sales tax reimbursement from the lessor. (See Reg. 1660, subd. (c)(2) and (3), regarding property purchased tax-paid and leased in substantially the same form as acquired.) And, staff explained that, with respect to sales tax transactions, the existing provisions of Regulation 1655 would apply to a manufacturer’s claim for a refund for sales tax reimbursement the manufacturer included in restitution paid to a lessor, under the Lemon Law. Furthermore, staff noted that AB 242 did not change the application of the Lemon Law to sales

tax transactions, and that questions regarding the application of Regulation 1655 to sales tax transactions were beyond the scope of the current interested parties process, which was to discuss the issue of whether to amend Regulation 1655 to clarify the new provisions of the Lemon Law applicable to use tax transactions.

Since BTC staff did not receive any other inquiries or comments regarding the draft amendments during or subsequent to the first interested parties meeting and staff had no changes to its recommendation to amend Regulation 1655, BTC staff did not prepare a second discussion paper and cancelled the second interested parties meeting that was previously scheduled to discuss staff's draft amendments. Staff also notified interested parties that comments could be submitted up to October 17, 2013, for consideration in the preparation of a Formal Issue Paper regarding the draft amendments. However, staff did not receive any other comments.

### *December 17, 2013 BTC Meeting*

Subsequently, staff prepared Formal Issue Paper 13-012 and distributed it to the Board Members for consideration at the Board's December 17, 2013, BTC meeting. Formal Issue Paper 13-012 recommended that the Board approve and authorize publication of the amendments to Regulation 1655 (discussed above) in order to incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle (as provided in Civ. Code, § 1793.2, subd. (d)(2)(D), as added by AB 242).
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund (consistent with Civ. Code, § 1793.25, subd. (a), as amended by AB 242).
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee (as provided in Civ. Code, § 1793.25, subd. (e), as added by AB 242).<sup>2</sup>

During the December 17, 2013, BTC meeting, the Board Members unanimously voted to propose the amendments to Regulation 1655 recommended in the formal issue paper. The Board determined that the proposed amendments to Regulation 1655 are reasonably necessary for the specific purpose of making the regulation consistent with and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242, and addressing the issue (or problem) that Regulation 1655 does not currently indicate that AB 242 made amendments to Civil Code sections 1793.2 and 1793.25.

The Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing

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<sup>2</sup> The formal issue paper also recommended that the Board approve a minor grammatical change capitalizing the first letter in the word "Board" in Regulation 1655, subdivision (b)(2)(B).

additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

The adoption of the proposed amendments to Regulation 1655 is not mandated by federal law or regulations. There is no previously adopted or amended federal regulation that is identical to Regulation 1655 or the proposed amendments to Regulation 1655.

#### DOCUMENTS RELIED UPON

The Board relied upon Formal Issue Paper 13-012, the exhibits to the issue paper, and the comments made during the Board's discussion of the issue paper during its December 16, 2013, BTC meeting in deciding to propose the amendments to Regulation 1655 described above.

#### ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed amendments to Regulation 1655 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 to Regulation 1655 at this time because the Board determined that the proposed amendments are reasonably necessary for the reasons set forth above.

The Board did not reject any reasonable alternative to the proposed amendments to Regulation 1655 that would lessen any adverse impact the proposed action may have on small business or that would be less burdensome and equally effective in achieving the purposes of the proposed action. No reasonable alternative has been identified and brought to the Board's attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purposes for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

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

Prior to the enactment of AB 242, the Lemon Law expressly provided that a manufacturer was required to make restitution to a buyer in an amount equal to the actual price paid or payable by the buyer, including *sales* tax. The Lemon Law further required the Board to reimburse a manufacturer for an amount equal to the *sales* tax which the manufacturer paid to or for a buyer when providing a replacement vehicle or making restitution. However, the Lemon Law did not expressly address the treatment of *use* tax.

As previously explained in more detail above, AB 242 made specific amendments to Civil Code sections 1793.2 and 1793.25. The amendments clarify that restitution, under the Lemon Law, includes *use* tax paid or payable by a buyer, including a lessee, of a new motor vehicle. The amendments also clarify that the Board is required to reimburse a manufacturer of a new motor vehicle for an amount equal to the use tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution pursuant to California's "Lemon Law." In addition, in order to claim reimbursement for such use tax, the amendments specifically require a manufacturer to provide satisfactory evidence that the buyer paid use tax on the sales price of or the lessee paid use tax on the rentals payable from the lease of the vehicle that the manufacturer replaced or made restitution for. And, the amendments specifically provide that, with regard to leases, the amount of use tax that the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee under the Lemon Law.

As previously explained in more detail above, subdivision (b)(2) of Regulation 1655 explains when manufacturers must provide restitution or a replacement vehicle to a buyer under the Lemon Law. Regulation 1655, subdivision (b)(2), also prescribes the requirements for a manufacturer to claim a refund from the Board for sales tax or sales tax reimbursement included in restitution paid to a buyer under the Lemon Law. However, Regulation 1655 does not indicate that AB 242 made amendments to the Lemon Law to clarify that restitution includes *use* tax paid or payable by a buyer or lessee of a new motor vehicle and require the Board to reimburse a manufacturer of a new motor vehicle for an amount equal to the *use* tax that the manufacturer is required to pay to or for a buyer or lessee when replacing a vehicle or making restitution.

Also, as previously explained above, the proposed amendments to Regulation 1655 incorporate the provisions of Civil Code sections 1793.2 and 1793.25, as amended by AB 242, by:

- Specifying that the term buyer includes a lessee of a new motor vehicle.
- Adding a reference to use tax, lease agreement, lessor, and lease where the current regulation refers to sales tax, sales agreement, dealer, and retail sale, respectively.
- Creating a list of the types of evidence that sales or use tax was paid, and requiring a manufacturer to provide one of the listed types of evidence when filing a claim for refund.
- Specifying that the amount of use tax that the Board is required to reimburse the manufacturer is limited to the amount of use tax the manufacturer is required to pay to or for the lessee.

As a result, the proposed amendments make Regulation 1655 consistent with the amendments made to the Lemon Law by AB 242, the proposed amendments do not mandate that individuals or businesses do anything that is not already required by the Lemon Law, and there is nothing in the proposed amendments that would significantly change how individuals and businesses would generally behave, in the absence of the proposed regulatory action, or that would impact revenue. Therefore, the Board estimates that the proposed amendments will not have a measurable economic impact on individuals and business that is in addition to whatever economic impact the amendments made to the Lemon Law by AB 242 have had and will have on individuals and businesses. The Board has determined that the proposed amendments to Regulation 1655 are not

a major regulation, as defined in Government Code section 11342.548 and California Code of Regulations, title 1, section 2000, because the Board has estimated that the proposed amendments will not have an economic impact on California business enterprises and individuals in an amount exceeding fifty million dollars (\$50,000,000) during any 12-month period. And, the Board anticipates that the proposed amendments to Regulation 1655 will promote fairness and benefit taxpayers, including manufacturers, Board staff, and the Board by providing additional notice regarding and implementing, interpreting, and making specific the amendments made to Civil Code sections 1793.2 and 1793.25, by AB 242.

In addition, based on these facts and all of the information in the rulemaking file, the Board has determined that the adoption of the proposed amendments to Regulation 1655 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 1655 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 1655 will not affect the benefits of Regulation 1655 to the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the proposed amendments to Regulation 1655 will not have a significant adverse economic impact on business.

The proposed amendments to Regulation 1655 may affect small businesses.

**Text of Proposed Amendments to  
California Code of Regulations, Title 18, Section 1655**

**1655. Returns, Defects and Replacements.**

**(a) Returned Merchandise.**

(1) In General. Except as provided in paragraph (2) of this subdivision, the amount upon which tax is computed does not include the amount charged for merchandise returned by customers if, (1) the full sale price, including that portion designated as "sales tax," is refunded either in cash or credit, and (2) the customer, in order to obtain the refund or credit, is not required to purchase other property at a price greater than the amount charged for the property that is returned. Refund or credit of the entire amount is deemed to be given when the purchase price, less rehandling and restocking costs, is refunded or credited to the customer. The amount withheld for rehandling and restocking may not exceed the actual cost of rehandling and restocking the returned merchandise. However, in lieu of using the actual cost for each transaction, the amount withheld for rehandling and restocking may be a percentage of the sales price determined by the average cost of rehandling and restocking returned merchandise during the previous accounting cycle (generally one year). If the seller elects to withhold rehandling and restocking amounts based on a percentage of sales price, the seller is bound by that election for the entire accounting cycle for which the election is made and must apply that percentage in lieu of actual cost during that period on all returned merchandise transactions for which rehandling and restocking costs are withheld. The amount withheld as rehandling and restocking costs may not include compensation for increased overhead costs because of the return, for refinishing or restoring the property to salable condition where the necessity therefore is occasioned by customer usage, or for any expense prior to the "sale" (i.e., transfer of title, lease, or possession under a conditional sale contract). Sellers must maintain adequate records which may be verified by audit, documenting the percentage used.

**(2) Contract Cancellation Options Required by Car Buyer's Bill of Rights.**

(A) Contract Cancellation Option. On and after July 1, 2006, the terms "gross receipts" and "sales price" do not include the purchase price for a contract cancellation option agreement with respect to a contract to purchase a used vehicle with a purchase price of less than forty thousand dollars (\$40,000), which a dealer is required to offer to a buyer pursuant to Vehicle Code section 11713.21. The purchase price for a contract cancellation option described in this subparagraph shall not exceed:

1. Seventy-five dollars (\$75) for a vehicle with a cash price of five thousand dollars (\$5,000) or less;
2. One hundred fifty dollars (\$150) for a vehicle with a cash price of more than five thousand dollars (\$5,000), but not more than ten thousand dollars (\$10,000);
3. Two hundred fifty dollars (\$250) for a vehicle with a cash price of more than ten thousand dollars (\$10,000), but not more than thirty thousand dollars (\$30,000); or

4. One percent of the purchase price for a vehicle with a cash price of more than thirty thousand dollars (\$30,000), but less than forty thousand dollars (\$40,000).

(B) Restocking Fee. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include the dollar amount of a restocking fee the buyer must pay to the dealer to exercise the right to cancel a purchase of a used car under a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph. The dollar amount of a restocking fee described in this subparagraph shall not exceed:

1. One hundred seventy-five dollars (\$175) if the vehicle’s cash price is five thousand dollars (\$5,000) or less;
2. Three hundred fifty dollars (\$350) if the vehicle’s cash price is more than five thousand dollars (\$5,000), but less than ten thousand dollars (\$10,000); or
3. Five hundred dollars (\$500) if the vehicle’s cash price is ten thousand dollars (\$10,000) or more.

(C) Amounts Refunded to Customers. On and after July 1, 2006, the terms “gross receipts” and “sales price” do not include that portion of the selling price for a used motor vehicle that is refunded to the buyer due to the buyer’s exercise of the right to return the vehicle for a refund, which is contained in a contract cancellation option agreement pursuant to Vehicle Code section 11713.21 as described in subparagraph (A) of this paragraph.

(b) Defective Merchandise.

(1) In General. Amounts credited or refunded by sellers to consumers on account of defects in merchandise sold may be excluded from the amount on which tax is computed. If, however, defective merchandise is accepted as part payment for other merchandise and an additional allowance or credit is given on account of its defective condition, only the amount allowed or credited on account of defects may be excluded from taxable gross receipts. The amount allowed as the “trade-in” value must be included in the measure of tax.

(2) Restitution or Replacement Under California Lemon Law.

(A) General. Under subdivision (d) of Civil Code section 1793.2, if a manufacturer is unable to service or repair a “new motor vehicle,” as that term is defined in subdivision (e)(2) of Civil Code section 1793.22, to conform to the applicable express warranties after a reasonable number of attempts, the manufacturer must either replace the motor vehicle or provide the buyer restitution of the purchase price, less specified amounts, at the buyer’s election.

For purposes of this regulation, the term buyer shall include a lessee of a new motor vehicle.

(B) Restitution. A manufacturer who pays a buyer restitution pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 is entitled to a refund of the amount of sales or use tax, or sales tax reimbursement included in the restitution paid by the manufacturer to the buyer. The manufacturer may file a claim for refund of that amount with the Bboard. The claim must include a statement that the claim is submitted in accordance with the provisions of section 1793.25 of the Civil Code. The manufacturer must submit with the claim documents evidencing that restitution was made pursuant to, and in complete compliance with, subdivision (d)(2) of Civil Code section 1793.2 including: a copy of the original sales or lease agreement between the buyer and the dealer or lessor of the non-conforming motor vehicle; copies of documents showing all deductions made in calculating the amount of restitution paid to the buyer along with full explanations for those deductions, including settlement documents and odometer statements; a copy of the title branded "Lemon Law Buyback" for the non-conforming motor vehicle returned by the buyer; and proof that the decal the manufacturer is required to affix to that motor vehicle has been so affixed in accordance with section 11713.12 of the Vehicle Code. The manufacturer must also submit with the claim the seller's permit number of the dealer or lessor who made the retail sale or lease of the non-conforming motor vehicle to the buyer, and evidence for one of the following:

1. that the dealer had reported and paid sales tax on the gross receipts from that sale; or
2. The buyer of the motor vehicle had paid the use tax on the sales price for the storage, use, or other consumption of that motor vehicle in this state; or
3. The lessee of the motor vehicle had paid the use tax on the rentals payable from the lease of the vehicle.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer restitution is not relevant for purposes of determining whether restitution has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(C) Replacement. For purposes of this regulation, a manufacturer who, pursuant to subdivision (d)(2) of Civil Code section 1793.2, replaces a non-conforming motor vehicle with a new motor vehicle substantially identical to the motor vehicle replaced is replacing the motor vehicle under the terms of the mandatory warranty. No additional tax is due unless the buyer is required to pay an additional amount to receive the replacement motor vehicle, in which case tax is due measured by the amount of that payment. If an amount is refunded to the customer as part of the exchange of the non-conforming motor vehicle for the replacement motor vehicle, then that amount is regarded as restitution for purposes of this regulation if it satisfies the requirements of subdivision (d)(2) of Civil Code section 1793.2. The manufacturer may file a claim for refund under subdivision (b)(2)(B) of this regulation for the amount of sales or use tax, or sales tax reimbursement that is included in the amount of that restitution paid by the manufacturer to the buyer.

For purposes of this regulation, the number of attempts made to repair the non-conforming motor vehicle, if any, prior to providing the customer a replacement is not relevant for purposes of determining whether the replacement has been made pursuant to subdivision (d)(2) of Civil Code section 1793.2.

(D) The amount of use tax the Board is required to reimburse the manufacturer shall be limited to the amount of use tax the manufacturer is required to pay to or for the lessee pursuant to Civil Code section 1793.2.

(c) Replacement Parts - Warranties.

(1) In General - Definitions. "Mandatory Warranty." A warranty is mandatory within the meaning of this regulation when the buyer, as a condition of the sale, is required to purchase the warranty or guaranty contract from the seller. "Optional Warranty." A warranty is optional within the meaning of this regulation when the buyer is not required to purchase the warranty or guaranty contract from the seller, i.e., the buyer is free to contract with anyone he or she chooses.

(2) Mandatory Warranties. The sale of tangible personal property includes the furnishing, pursuant to the guaranty provisions of the contract of sale, or mandatory warranty, of replacement parts or materials, and if the property subject to the warranty is sold at retail, the measure of the tax includes any amount charged for the guaranty or warranty, whether or not separately stated. The sale of the replacement parts and materials to the seller furnishing them thereunder is a sale for resale and not taxable.

(3) Optional Warranties. The person obligated under an optional warranty contract to furnish parts, materials, and labor necessary to maintain the property is the consumer of the materials and parts furnished and tax applies to the sale of such items to that person. If he or she purchased the property for resale or from outside California, without tax paid on the purchase price, he or she must report and pay tax upon the cost of such property to him or her when he or she appropriates it to the fulfillment of the contract of warranty.

(4) Deductibles. A deductible paid by a customer under the terms of a mandatory or optional warranty contract is subject to tax measured by the amount of the deductible allocable to the sale of tangible personal property to the customer. For example, if the itemized sales price of tangible personal property (or the fair retail value if not separately itemized) provided pursuant to a warranty is 50 percent of the total fair retail value of the repairs and the deductible is \$100, 50 percent of that deductible, \$50, would be allocable to the sale of tangible personal property and would be subject to tax, whether the warranty were optional or mandatory. Unless otherwise stated in the warranty contract, when either an optional or a mandatory warranty provides that the customer will pay a deductible towards repairs and services provided under the warranty, the person providing the warranty contract is liable for any tax or tax reimbursement otherwise payable by the customer with respect to that deductible.

Note: Authority cited: Section 7051, Revenue and Taxation Code. Reference: Sections 6006-6012 and 6012.3, Revenue and Taxation Code; Sections 1793.2-1793.25, Civil Code; and Sections 11713.12 and 11713.21, Vehicle Code.

## Regulation History

**Type of Regulation:** Sales and Use Tax

Regulation: 1655

Title: 1655, *Returns, Defects and Replacements*

**Preparation:** Monica Silva

**Legal Contact:** Monica Silva

The proposed amendments to Regulation 1655, *Returns, Defects and Replacements*, clarify that the regulation's provisions regarding restitution and replacement under the "Lemon Law" apply to use tax under specified circumstances.

### History of Proposed Regulation:

April 22-24, 2014	Public Hearing
February 14, 2014	OAL publication date; 45-day public comment period begins; Interested Parties mailing
February 4, 2014	Notice to OAL
December 17, 2013	Business Tax Committee, Board Authorized Publication (Vote 5-0)

**Sponsor:** NA

**Support:** NA

**Oppose:** NA