STATE BOARD OF EQUALIZATION
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April 25, 2017

Mr. [Begin deleted text REDACTED TEXT End deleted text, Senior Vice President

Re: Tax Opinion Request 16-413
Unidentified Taxpayer

Dear Mr. Begin deleted text REDACTED TEXT End deleted text

This is in response to your letter dated July 1, 2016, in which you request clarification of Tax Opinion 10-493 regarding the application of the Sales and Use Tax Law to the deposit required to be collected from consumers on the sale of small containers of automotive refrigerant under the recycling program established by California Code of Regulations, title 17, sections (ARB Regulation or ARB Reg.) 95360-95370.

You state, in relevant part:

[Tax Opinion 10-493] uses Revenue and Taxation section 6364 to determine if the can deposit is taxable. Subsection (e) of section 6364 defines "returnable container" as a container customarily returned for reuse: "(e) For purposes of this section, returnable containers means containers of a kind customarily returned by the buyer of the contents for reuse (emphasis added). All other containers are nonreturnable containers." I believe that BOE might have applied the incorrect provision of the tax code in the case of a small refrigerant can since that can is in fact not reused, but crushed and recycled after the refrigerant is removed.

A more appropriate reference point for the small refrigerant can may be an automotive part core which is returned to the retailer or service facility for remanufacturing into a new part. According to Section 4 of BOE's Auto Repair Shop guidance (BOE Publication 25, "Auto Repair Garages and Service Stations" which is attached), shops are advised not to return the sales tax on a core that is returned. The booklet states: "When giving your customer a refund of the core charge for bringing in a used part, do not refund the tax you collected on the charge." While the booklet does not cite a particular regulation for this statement, this conclusion is apparently based on Cal. Code Regs., tit. 18 § 1655 which governs sales tax on returns. This section instructs that where sales tax is collected on the entire amount of a sale, the sales tax is refunded only if the entire amount of the sale is reversed. Under this section, sales tax is properly collected on the

entire amount of the sale of a part and, because the entire amount of the sale is not refunded to the customer, there is no return of sales tax when the core is returned.

At this time it appears that there is some confusion in the retailer community as to the tax status of the small refrigerant can. This confusion is compounded by the fact that CARB is forwarding the 2011 BOE letter which appears to contradict the guidance that BOE has provided regarding the taxation of cores. Therefore, I am requesting that your agency review the guidance it has provided to determine whether in fact the deposit portion on the sale of a small can of refrigerant is taxable or not.

I have also discussed this matter with representatives of the California Air Resources Board (ARB), Begin deleted text REDACTED TEXT End deleted text, on November 30, 2016, and discussed this matter again with Mr. Begin deleted text REDACTED TEXT End deleted text on January 5, 2010. They confirmed that it was their understanding as well that once excess refrigerant was removed from the cans by the manufacturers the cans were simply recycled and not refilled or otherwise reused by the manufacturer.

I have also reviewed the ARB website for materials related to the recycling program, including the Final Statement of Reasons, dated July 21, 2009, and the Addendum to the Final Statement of Reasons, dated January 5, 2010. I have also reviewed materials related to proposed amendments to the applicable ARB regulations, including ARB Resolution 16-5, Proposed Amendments to the Small Containers of Automotive Refrigerant Resolution, dated April 22, 2016.

The analysis and conclusions in this letter are based on the facts and representations made in your July 1, 2016, letter and on the additional information and materials discussed above as well as on any assumptions stated herein. Since this request seeks further clarification of Tax Opinion 10-493, I have enclosed a copy of that opinion, and it is incorporated by reference herein.

I also note that Revenue and Taxation Code section 6596 sets forth the circumstances under which a taxpayer may be relieved of liability for taxes when relying on a written response to a written request for advice from the Board. This opinion does not come within section 6596 because the identity of the specific person for whom the advice is requested was not disclosed in this request for written advice. (See Cal. Code Regs., tit. 18, § (Regulation or Reg.) 1705, subd. (b)(1).)

DISCUSSION

As a starting point, California imposes a sales tax measured by a retailer's gross receipts from the retail sale of tangible personal property inside this state, unless the sale is specifically exempted from taxation by statute. (Rev. & Tax. Code, §§ 6051, 6091.) The sales tax is imposed on the retailer who may collect reimbursement from its customer if the contract of sale so provides. (Civ. Code, § 1656.1; Reg. 1700.) When sales tax does not apply, use tax is imposed, measured by the sales price of property purchased from a retailer for the storage, use, or other consumption of the property in California, unless specifically exempted or excluded from taxation by statute. (Rev. & Tax. Code, §§ 6201, 6401.) The use tax is imposed on the person actually storing, using, or otherwise consuming the property. (Rev. & Tax. Code, § 6202.) "Gross receipts," for the purposes of the sales tax, and "sales price," for the purposes of the use

tax, include all amounts received with respect to the sale, with no deduction for the cost of the materials used, labor or service cost, or any other expense of the retailer passed on to the purchaser. (Rev. & Tax. Code, §§ 6011, 6012.)

As discussed in more detail in Tax Opinion 10-493, ARB Regulations 95360 through 95370 implement a recycling program for small containers of automotive refrigerant. Specifically, ARB Regulation 95366 describes the container deposit and return program. It states, in relevant part:

> (a) Except for small containers of automotive refrigerant exempted under section 95363 or section 95364 of this subarticle, on or after January 1, 2010, and subject to the provisions of section 95367, a retailer of automotive refrigerant in a small container that is subject to the requirements of this subarticle must:
>
> > (1) Collect a deposit from the consumer or charge the consumer's account for each small container of automotive refrigerant at the time of sale.
> >
> > (2) The amount of deposit on each small container is initially set at $10, and can be increased in $5 increments as described in section 95367(d)(1) or decreased in $5 decrements as described in section 95367(d)(2), but in no event shall the deposit amount of section 95366(a) be reduced below $5.
> >
> > (3) Return the deposit to the consumer, or credit the consumer's account when the consumer returns a used small container of automotive refrigerant to the retailer, provided that the consumer returns the used container of refrigerant to the retailer where purchased within 90 days of purchase, submits proof of purchase (e.g., cash register receipt), and provided that the container has not been breached. A retailer may return the deposit at his discretion if more than 90 days have elapsed, the consumer does not have a receipt, if the consumer returns the container to a location other than the place of purchase, or if the container has been breached.
>
> (b) Except for small containers of automotive refrigerant exempted under section 95363 or section 95364 of this subarticle, on or after January 1, 2010, and subject to the provisions of section 95367, a manufacturer or its designated return agency must:
>
> > (1) Collect a deposit on each small container of automotive refrigerant at the time of sale to a distributor or retailer.
>
> (e) A manufacturer or its designee must recover any refrigerant remaining in the returned small containers at a facility registered with the ARB as described in "Certification Procedures for Small Containers of Automotive Refrigerant" adopted on July 20, 2009, and last amended on January 5, 2010, which is incorporated by reference herein. The facility must employ good engineering

> practices to avoid loss of refrigerant to the atmosphere. The refrigerant must be recovered, recycled, reclaimed, or removed to a licensed waste disposal facility.

The ARB is required to calculate and publish annual rates of return of the containers by consumers, and increase the amount of the deposit if the rate is lower than the target rate, 95 percent as of January 1, 2012, or decrease the amount of the deposit if it exceeds the target rate. (ARB Reg. 95367, subd. (b)-(d).) According to Resolution 16-5, proposing amendments to the ARB regulations, the recycle rate of 70 percent achieved from 2011 to 2014 is in fact sufficient to achieve the emissions reduction goals of the program, and the ARB is therefore proposing amendments to ARB regulation 95366, subdivision (a), fixing the amount of the deposit at $10.

ARB regulation 95366, subdivision (b), does not establish the amount of the deposit collected by manufacturers. As stated in the ARB's Final Statement of Reasons, response to comment 16:

> [S]taff was fully aware that the container deposit program would consist of two separate deposits, the deposit a retailer would pay a manufacturer when purchasing new containers, and the deposit a consumer would pay the retailer at the time of purchase. Both these deposits would be refunded when the used containers were returned for recycling. However, the Agency elected to only establish a minimum amount for the retailer-consumer deposit because it believed that manufacturers and retailers are better situated to establish and administer the manufacturer-retailer deposits.

According to Resolution 16-5, the intent of the program is to direct all unclaimed deposits retained by manufacturers, distributors, and retailers to a manufacturer-managed account used to fund enhanced education programs for the benefit of consumers. Manufacturers are explicitly required to report the amounts of unclaimed deposits retained, and provide an accounting and description of how those funds are spent to enhance consumer education. (ARB Reg. 95367, subd. (a)(5).) The ARB is therefore proposing amendments to ARB regulation 95366, subdivision (a)(4), clarifying the existing requirement that retailers must transfer unclaimed consumer-retailer container deposits to the manufacturers who would in turn expend such deposits to fund consumer education programs or other programs, projects, and measures reducing greenhouse gas emissions, as approved by the ARB.

In Tax Opinion 10-493, we concluded that the deposit charged by retailers to consumers described in ARB Regulation 95366, subdivision (a), was a "deposit" as defined by Regulation 1589 charged on a returnable container and therefore not subject to tax pursuant to Regulation 1589, subdivision (b).[1] This was based on our understanding that the containers were reused, i.e. refilled with refrigerant and resold. As stated in your letter, and as confirmed by representatives of the California Air Resources Board, this is not the case; the containers are in fact not reused within the meaning of Regulation 1589. Rather, after the excess refrigerant is removed the containers are simply discarded or recycled, i.e. crushed, melted or otherwise reprocessed into raw materials. As such, because the container is not a reusable container as

[1] A "returnable container" is a container of a kind customarily returned or resold by the buyers of the content for re-use by the packers, bottlers or sellers of the commodities contained therein. (Rev. & Tax. Code, § 6364, subd. (e); Reg. 1589, subd. (a).) A container, title to which is retained by the seller or for which a deposit is taken by such seller, is a returnable container. (Reg. 1589, subd. (a).)

defined in Regulation 1589, the amount charged by the retailer pursuant to ARB Regulation 95366, subdivision (a), is not a "deposit" as defined under Regulation 1589. (See *Associated Beverage Co. v. Bd. of Equalization* (1990) 224 Cal.App.3d 192, 198.) Nonetheless, as we explain below, we still find that the deposit charged by retailers to consumers pursuant to ARB Regulation 95366, subdivision (a), is not subject to sales or use tax because it is not includable in "gross receipts" or in the "sales price."

As stated above, "gross receipts," for the purposes of the sales tax, and "sales price," for the purposes of the use tax, include all amounts received with respect to the sale, with no deduction for the cost of the materials used, labor or service cost, or any other expense of the retailer passed on to the purchaser. (Rev. & Tax. Code, §§ 6011, 6012.) Unlike an expense of the retailer passed on to the purchaser, a charge imposed by a government entity on the purchaser and collected by the retailer is not included in taxable gross receipts or sales price. (See, e.g., Sales and Use Tax Annotation[2] (Annotation or Annot.) 295.1237 (2/24/05, 2006-1).) Even if a portion of the charge may be retained by the retailer, it does not change the analysis that such a charge imposed on a purchaser is not included in taxable gross receipts. (See, e.g., Annot. 295.1302.500 (3/21/2000, Am. 2000-3).)

Here, ARB regulation 95366, subdivision (a)(1), requires that retailers "collect a deposit from the consumer or charge the consumer's account for each small container of automotive refrigerant at the time of sale." The deposit is intended to ensure that customers return the used containers at the target rate. Additionally as discussed in ARB Resolution 16-5, the intent of the container deposit and return program was to direct all unclaimed deposits retained by the retailers to a manufacturer-managed account used to fund enhanced education programs for the benefit of consumers. In other words, the deposit is intended to affect the behavior of consumers and retailers are not intended to receive any benefit from unclaimed deposits.

Additionally, although ARB regulation 95366, subdivision (b), also requires a manufacturer to collect a deposit from the retailer, this is a separate charge from the deposit at issues, which is imposed on the customers. Therefore, the deposit at issue does not represent the cost of the deposit imposed on the manufacturer being passed down to the consumer.[3] The amount of the deposit collected from the retailer by the manufacturer could be as little as .1 percent ($.01/$10.00) of the deposit collected from the consumer by the retailer. Additionally, the Final Statement of Reasons promulgated by the ARB makes explicitly clear that these are two separate deposits.

Under these circumstances, based on the language of ARB regulation 95366, subdivision (a)(1), and consistent with the annotations cited above, the deposit is imposed on the consumer; it is not an expense of the retailer that is passed on to the customer. Retailers have an obligation to collect the deposit, but it is the intent of the program that all unclaimed deposits retained by the retailers be remitted to a manufacturer-managed account used to fund enhanced education programs for the benefit of consumers. Consequently, the deposits are not part of a retailer's gross

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[2] Annotations are summaries of the conclusions reached in selected opinions of attorneys of the Board's Legal Department and are intended to provide guidance regarding the interpretation of Board statutes and regulations as applied by staff to specific factual situations. (See Reg. 5700.)

[3] In contrast, for example, the CRV, the amount representing redemption or recycling values of beverages pursuant to division 12.1 of the Public Resources Code, is explicitly imposed on the distributor but may be passed on all the way to the consumer. (Pub. Resources Code. §§ 14560, 14560.5.)

receipts or of the sales price from the sale of small containers of automotive refrigerant and are therefore not included in the measure of tax.

As a final note, the "core charges" discussed in Publication 25, *Auto Repair Garages and Service Stations*, are not a useful analog for this analysis because they are not imposed by an outside public agency. Moreover, the guidance provided by Publication 25 related to core charges on new and reconditioned or rebuilt parts is based on the application of Regulation 1546, *Installing, Repairing, Reconditioning in General*, which has no bearing on the present discussion. (See, e.g., Annot. 315.0370 (2/27/80).)

I trust that this suffices to answer your questions. If you have any further questions, please write again.

Sincerely,

Scott Claremon
Tax Counsel III (Specialist)

SAC/yg

cc: Out-of-State District Administrator (OH)