

**Levine, David**

330.2297

**From:** Levine, David  
**To:** Khabbaz, Leila  
**Cc:** Anderson, Vic;  
**Subject:** 330.2297 (7/16/81)  
**Date:** Friday, September 26, 1997 10:19AM

I think this annotation needs some clarification. The annotation (and backup) indicate that the notice is "inappropriate." When I first looked at it, I thought, why shouldn't this statement in the invoice relieve the lessee of liability?" In fact, it appears that the requirements in subdivision (b) of Regulation 1686 are not for the purpose of relieving the lessee of tax no matter what. Rather, the provision appears designed to ensure that, if the lease isn't taxable, the lessor notify the lessee of the facts supporting nontaxability. If the notice is wrong, the lessee is still liable for the tax, but the giving of the notice should put the lessor on the hook for indemnity to the lessee, as indicated in this annotation. Thus, it does not appear that the lessee remains liable for the tax because the notice was "inappropriate" and "erroneous," but rather because the lessee's liability is simply unaffected by ANY notice under Regulation 1686(b), whether correct or not. The notice does not act as an exemption certificate. Rather, it is simply a duty imposed on the lessor to explain why it isn't collecting tax from the lessee. If notice is correct, the lessee does not owe tax because the lease is not, in fact, a sale, not because the lessee received a notice. If the notice is wrong, the lessee remains on the hook. However, if such is the case, since the notice would be part of the lease contract, it is my opinion that the lessee would have indemnity rights against the lessor based on that notice even if it did not have the explicit statement to that effect as did the notice discussed in this annotation.

I suggest this annotation be rewritten to clarify that the notice given under 1686(b) is simply to provide info to the lessee, and does not, itself, serve to relieve the lessee of liability for tax. I don't think the annotation should not use the term "inappropriate" because it is misleading in this context.

**M e m o r a n d u m****330.2297**

To: Mr Robert Nunes

Date: July 16, 1981

From: Gary J. Jugum

Subject: Liability for tax on leases

This is in response to your memorandum of July 13, 1981.

We understand that the lessee of certain tangible personal property has entered into an agreement with its lessor which provides, with respect to California rentals, as follows:

“... if ‘Rental Not Taxable’ has been checked on the face of this Agreement, Lessor warrants that Lessor has paid sales tax pursuant to Section 6052 of the California Revenue Taxation Code or has paid use tax measured by the purchase price of the equipment and that the equipment is in substantially the same form as acquired; Lessor will indemnify Contractor against any sales or use taxes that may be claimed to be due in connection with this lease or the rentals or other payments hereunder.”

The quoted language does not “require” that the lessor pay tax upon its purchase price of the equipment. This term is only a statement by the lessor that tax was paid on cost and a promise of indemnity if this statement is false. If tax has not been paid on cost, the lessee remains liable for use tax measured by rental receipts. However, the lessor has a contractual obligation to the lessee to indemnify the lessee.

Regulation 1686, paragraph (b) (2), has no application in the case in question. That paragraph only applies “for lease or rental transactions with respect to which use tax does not apply.” [Emphasis added.] In the case in question there is a representation that tax was not in fact paid on cost. The “notice” was inappropriate, and the liabilities of the lessor and the lessee vis-à-vis the taxing authority are not affected by the erroneous “notice.”

J:alicetilton