State of California

Board of Equalization
Legal Division-MIC: 82

M e m o r a n d u m

580.0077

To : Mr. Dan Cady, Supvg. Tax Aud. II
Loc. Rev. Alloc. Sect. (MIC:27)

Date: September 10, 2000

From : John L. Waid
Senior Tax Counsel

Telephone: (916) 324-3828

Subject: SR - -- XX-XXXXXX
[F] --- --- ---

I am answering your memorandum to me dated June 19, 2001. You ask about the allocation of local tax revenue under the peculiar fact pattern in this case. You set forth the factual background as follows:

> "--- --- --- ---. [F] is a subsidiary wholly owned corporation of an insurance company. [F] has entered into two contracts with its parent corporation, [B]: Motor Vehicle Lease Contract … dated December 20, 1967 and Management Contract … dated January 2, 1968 both negotiated at Corporate headquarters [in] Los Angeles. [The Lease Contract] establishes the lease provisions for automobiles leased to [F] Companies which in turn provide the leased vehicles free of charge to their employees who are attorney(s) and claim adjusters (Group A employees), but not involved in the sale of insurance. [The Management Contract] identifies how the lease business activities will be conducted between [F] and related parties. [F] also leases a few motor vehicles to its employees who are neither attorney(s) nor claim adjuster(s) (Group B employees) but conduct leasing activities. Group A and B employees have the option to buy the leased vehicles either after 2 years of use or after reaching a number of miles on the leased vehicles. [F] leases new motor vehicles only on a long term basis, but does not lease to the general public.
>
> "… Automobile lease orders are taken [in] Los Angeles where --- and parent companies office is located. The Board of Directors of --- Underwriters Association approves all vehicle lease orders. All vehicle orders by --- are placed though out-of-state motor vehicle dealers who forward these to the respective manufacture. The automobiles are courtesy delivered though local California vehicle dealers nearest to the destination of the Group A and B employees. However, all leased vehicles are registered in the names of respective insurance companies."

You indicate that [F] had been allocating local tax (use tax presumably) through the countywide pools from 1Q96 though 4Q97 until the Allocation Group advised it to allocate all local taxes to Los Angeles, where it is located. You ask several questions about the applicability and allocation of local tax.

Taking the easy issues first, you indicate that the people who receive the vehicles have the option to purchase the leased vehicles at a reduced book value that is greater than a nominal value. [F] apparently does not pay tax when the vehicles are sent to the person driving it. Thus, [F]'s leases to its employees are straight-ahead leases under Regulation 1660(b)(2). The local use tax derived from them should be reported to the location of the vehicle through the medium of the countywide pool. When [F] sells the vehicles, the local sales tax should be reported to Los Angeles under Regulation 1802(a)(1).

Unfortunately, it is not possible to give you a definitive opinion regarding the leases to [B] at this time due to the lack of certain facts. We agree with you that, under Regulation 1660(c)(1), when the lessee is not subject to use tax, the applicable tax is sales tax measured by the rentals payable. As you note, [F] is leasing cars to employees of its parent insurance company. [F] is a wholly-owned subsidiary of [B], an insurance company, exempt under the State Constitution from sales or use tax. A parent and its wholly-owned subsidiaries are two separate legal persons. (See, *N. W. Pac. R. R. v. St. Bd. of Equal*. (1943) 21 Cal.2d 524, 530.) As a result, exemptions that apply to one do not apply to the other automatically. For the insurance-company exemption to apply, the tax must be levied on the insurance company itself. (See, e.g., *Benef. Std. Life Ins. Co. v. St. Bd. of Equal*. (1962) 199 Cal.App.2d 18, 22.)

[F] is not in the business of selling insurance but of leasing cars. Thus, the insurance-company exemption does not apply to [F]. It is liable for sales tax on these leases but only if it is the retailer.

Therein, as they say, lies the rub. It is not clear who is the retailer here. You indicate that [F] places its orders through out-of-state retailers who forward them to the respective manufacturers (presumably also out of state). Delivery, however, is made from the stock of a dealer in this state. We have previously concluded that where a licensed California dealer makes a "courtesy delivery" of a motor vehicle pursuant to a retail sale made by a person who is not a licensed California dealer, and the sale and registration is reported to the Department of Motor Vehicles on the Dealer's Report of Sale form, the dealer will be liable for sales tax measured by the retail selling price of the vehicle. (Annot. 580.0160 (7/17/64).) Two things are unclear in the facts we have. [F] is presumably not a licensed California dealer, but the facts do not indicate. If so, then the dealer would be selling to [F] for resale and [F] would report the tax. Likely, the dealer reports the transfer to DMV on its report of sale, but, again, the facts do not say. Neither the Lease Contract nor the Management Contract speaks to these issues.

Therefore, if [F] is the retailer, since the Los Angeles office seems to be its lone business location, the sales tax revenue from these leases should be allocated to Los Angeles under Regulation 1802(a)(1). If the car dealer that delivers the car is the retailer, however, the local sales tax revenue should be allocated to the dealer's location under the same authority.

JLW:sr

cc: Jim Stillwell (MIC:82)

State of California

Board of Equalization
Legal Division-MIC: 82

M e m o r a n d u m

580.0077

To :

Mr. Dan Cady
Supervising Tax Auditor
Local Revenue Allocation Section – MIC: 27

Date: April 5, 2002

From : John L. Waid
Senior Tax Counsel – MIC:82

Telephone: (916) 324-3828

Subject: SR - -- XX-XXXXXX
[F]

I am answering your memorandum to me dated February 8, 2002, following up on our earlier correspondence. In my memorandum to you dated June 19, 2001, I indicated that if [F] were not a California dealer and the dealers that make courtesy deliveries for it report the sale and registration to DMV on their own Reports of Sale (ROS), those dealers would be liable for sales tax measured by the retail selling price of the vehicles.

In your memorandum, you confirmed that [F] does not have a California new car dealer's license and that the dealers making courtesy deliveries for it do report the transactions to DMV on their own ROS'. As a result, the dealers are considered the retailers and must report the local sales tax revenue derived from such sales to the cities where they are located.

JLW:ljt

cc: Mr. Jim Stillwell – MIC:82

State of California

Board of Equalization
Legal Department-MIC: 82

M e m o r a n d u m

580.0077

To : Mr. Dan Cady
Supervising Tax Auditor
Local Revenue Allocation Section (MIC:27)

Date: August 19, 2003

From : John L. Waid
Senior Tax Counsel, (MIC:82)

Telephone: (916) 324-3828

Subject: **[F]**
Factory-Directed Courtesy Deliveries
SR - -- XX-XXXXXX

I am answering your memorandum to me dated May 9, 2003. You are following up on our earlier correspondence.

You are concerned about the conclusion of the Legal Department as expressed in my April 5, 2002, memorandum to you that the in-state car dealers are the retailers of the cars in the transactions at issue. You questioned this conclusion regarding the leases to Group A employees (attorneys and claims adjusters who are not involved in the sale of insurance and are provided the cars free of charge).

You state that your previous memorandum did not bring up that the vehicles leased to Group A employees were factory-directed courtesy deliveries through California dealers. It also did not note that the vehicles sold to the taxpayer were not delivered from California inventories. The in-state dealers would likely not be considered the retailers, because they did not negotiate the sales of the leased cars to the taxpayer.

The taxpayer currently reports use tax on these transactions. The identity of the retailer controls what tax applies, who reports it, and to what local jurisdictions the local tax revenues should go.

OPINION

You attached to your memorandum the back up memoranda for Annotation 580.0160 (7/17/64), which reads as follows:

> "Where a licensed California dealer makes a 'courtesy delivery' of a motor vehicle pursuant to a retail sale made by a person who is not a licensed California dealer, and the sale and registration is reported to the Department of Motor Vehicles on the Dealer's Report of Sale form, the dealer will be liable for sales tax measured by the retail selling price of the vehicle."

This annotation is based on former section 6389, which required that the gross receipts from retail sales of motor vehicles by licensed auto dealers be included in the measure of tax for sales tax purposes. (Unless otherwise stated, all statutory citations are to the Revenue and Taxation Code.) Section 6389 was enacted by Statutes 1963, Chapter 1858, section 5, operative October 1, 1963. It was repealed by Statutes 1965, First Extraordinary Session, Chapter 2, section 18, operative August 1, 1965. It was substantially re-enacted as section 6282 by section 14 of the same bill, operative July 1, 1966. Thus, despite the repeal of the cited statutory authority, the annotation still appears to be good law.

In our previous correspondence, you did confirm that the dealers making the courtesy deliveries do report the sales of the cars to the taxpayer on their Report of Sale (ROS) forms. As we understand it, the ROS doubles as the registration application. You had also indicated that both the Groups A and B employees who drive the cars have the option of buying them after two years or a certain amount of miles are reached. From the word "option," we conclude that the taxpayer sells the cars to other persons if the drivers do not buy them. The taxpayer qualifies as a lessor-retailer under Vehicle Code section 373(a), because it sells vehicles to persons other than the lessees or other persons designated by the lessees as the vehicles' drivers. It is thus licensed as such (presumably) under the Vehicle Code.

Under Regulation 1610(b)(1)(A), sales tax applies when the retailer is, among others, a lessor-retailer subject to the provisions of Vehicle Code section 11615.5. That section provides that it is unlawful for a person licensed under Vehicle Code section 11600 et. seq. as a lessor-retailer to make a retail sale of a motor vehicle without reporting and paying sales tax under section 6451 if he files the ROS. The taxpayer here, though, is leasing the cars, not selling them, and it does not file the ROS. Consequently, the regulation does not apply to make the taxpayer the retailer required to pay sales tax.

Dealers, on the other hand, are licensed under Vehicle Code section 11700 et. seq. The annotation is based on Vehicle Code 11713(m) (now 11713(l), which provides that it is unlawful for a dealer to participate in any sale of a motor vehicle reported to the DMV on an ROS without reporting and paying sales tax as required by section 6451. Thus, a dealer does not actually have to make the sale to be liable for sales tax, as does a lessor-retailer. The back-up memorandum concluded that by making the courtesy delivery and filing the ROS on a sale, the dealer "participated" in the sale within the meaning of the Vehicle Code and so was liable for the sales tax on the sale.

We conclude that, under this fact pattern, Vehicle Code section 11713(l) makes the dealers the retailers of the leased cars. Apparently, the manufacturer is making a sale for resale to the taxpayer. The Vehicle Code section does not, however, distinguish between retail sales and sales for resale. Those are sales tax concepts. Vehicle Code section 11713(l) merely says "sales." Thus, we confirm our previous opinion.

Audit Manual 608.55, which defines "factory-directed courtesy delivery," notes that these kinds of sales are "very often" not reported on the dealer's ROS. In cases where the delivering dealers do not report the sales on their own ROS', the results might be different. Where the delivering dealer files the ROS, however, he is avowing that he made the sale. (See, also, Reg. 1566(a).)

We must correct a factual error in our memorandum to you dated September 10, 2001. There we concluded that the taxpayer was leasing cars to the employees of its parent insurance company. This is not correct. The taxpayer is leasing the cars directly to sister subsidiaries that in turn provide the cars free of charge to the Group A employees. It does not, however, change our conclusion. The dealers make the courtesy deliveries and report the sales on their own ROS'. Under the annotation, then, the dealers sufficiently participate in the sales to require them to report and pay sales tax on the transactions. Thus, the local sales tax is reported to the local jurisdiction in which the dealer making the courtesy delivery is located. Use tax would not be due at all.

JLW/ef