

**Initial Statement of Reasons for the Adoption of  
California Code of Regulations, Title 18, Section 3802,  
Gross Receipts from Sales of Cannabis and Cannabis Products,  
With Proposed Amendments**

**SPECIFIC PURPOSES, PROBLEMS INTENDED TO BE ADDRESSED, NECESSITY, AND  
ANTICIPATED BENEFITS**

Current Law

*Sales Tax*

Sales tax is imposed on retailers for the privilege of selling tangible personal property at retail in California, and the rate of the sales tax applies to retailers' gross receipts from the sale of tangible personal property sold at retail in this state. (Rev. & Tax. Code (RTC), § 6051.) RTC section 6012 provides that, for sales tax purposes:

(a) "Gross receipts" mean the total amount of the sale or lease or rental price, as the case may be, of the retail sales of retailers, valued in money, whether received in money or otherwise, without any deduction on account of any of the following:

(1) The cost of the property sold. However, in accordance with any rules and regulations as the [Department<sup>1</sup>] may prescribe, a deduction may be taken if the retailer has purchased property for some other purpose than resale, has reimbursed his or her vendor for tax which the vendor is required to pay to the state or has paid the use tax with respect to the property, and has resold the property prior to making any use of the property other than retention, demonstration, or display while holding it for sale in the regular course of business. If that deduction is taken by the retailer, no refund or credit will be allowed to his or her vendor with respect to the sale of the property.

(2) The cost of the materials used, labor or service cost, interest paid, losses, or any other expense.

(3) The cost of transportation of the property, except as excluded by other provisions of this section.

(4) The amount of any tax imposed by the United States upon producers and importers of gasoline and the amount of any tax imposed pursuant to Part 2 (commencing with Section 7301) of this division.

---

<sup>1</sup> The administration of the Sales and Use Tax Law (SUTL) (RTC, § 6001 et seq.), Cannabis Tax Law (CTL) (RTC, § 34010 et seq.), and Fee Collection Procedures Law (FCPL) (RTC, § 55001 et seq.) was transferred from the State Board of Equalization (Board) to the California Department of Tax and Fee Administration (Department), operative July 1, 2017, by Assembly Bill No. (AB) 102 (Stats. 2017, ch. 16) and references to the "Board" in the SUTL, CTL, and FCPL statutes discussed herein mean the "Department" pursuant to Government Code (GC) section 15570.24 and RTC section 20.

(b) The total amount of the sale or lease or rental price includes all of the following:

(1) Any services that are a part of the sale.

(2) All receipts, cash, credits and property of any kind.

(3) Any amount for which credit is allowed by the seller to the purchaser.

(c) "Gross receipts" do not include any of the following:

(1) Cash discounts allowed and taken on sales.

(2) Sale price of property returned by customers when that entire amount is refunded either in cash or credit, but this exclusion shall not apply in any instance when the customer, in order to obtain the refund, is required to purchase other property at a price greater than the amount charged for the property that is returned. For the purpose of this section, refund or credit of the entire amount shall be deemed to be given when the purchase price less rehandling and restocking costs are refunded or credited to the customer. The amount withheld for rehandling and restocking costs may be a percentage of the sales price determined by the average cost of rehandling and restocking returned merchandise during the previous accounting cycle.

(3) The price received for labor or services used in installing or applying the property sold.

(4) (A) The amount of any tax (not including, however, any manufacturers' or importers' excise tax, except as provided in subparagraph (B)) imposed by the United States upon or with respect to retail sales whether imposed upon the retailer or the consumer.

(B) The amount of manufacturers' or importers' excise tax imposed pursuant to Section 4081 or 4091 of the Internal Revenue Code for which the purchaser certifies that he or she is entitled to either a direct refund or credit against his or her income tax for the federal excise tax paid or for which the purchaser issues a certificate pursuant to Section 6245.5.

(5) The amount of any tax imposed by any city, county, city and county, or rapid transit district within the State of California upon or with respect to retail sales of tangible personal property measured by a stated percentage of sales price or gross receipts whether imposed upon the retailer or the consumer.

(6) The amount of any tax imposed by any city, county, city and county, or rapid transit district within the State of California with respect to the storage, use or other consumption in that city, county, city and county, or rapid transit district of tangible personal property measured by a stated percentage of sales price or purchase price, whether the tax is imposed upon the retailer or the consumer.

(7) Separately stated charges for transportation from the retailer's place of business or other point from which shipment is made directly to the purchaser, but the exclusion shall not exceed a reasonable charge for transportation by facilities of the retailer or the cost to the retailer of transportation by other than facilities of the retailer. However, if the transportation is by facilities of the retailer, or the property is sold for a delivered price, this exclusion shall be applicable solely with respect to transportation which occurs after the sale of the property is made to the purchaser.

(8) Charges for transporting landfill from an excavation site to a site specified by the purchaser, either if the charge is separately stated and does not exceed a reasonable charge or if the entire consideration consists of payment for transportation.

(9) The amount of any motor vehicle, mobilehome, or commercial coach fee or tax imposed by and paid to the State of California that has been added to or is measured by a stated percentage of the sales or purchase price of a motor vehicle, mobilehome, or commercial coach.

(10) (A) The amount charged for intangible personal property transferred with tangible personal property in any technology transfer agreement, if the technology transfer agreement separately states a reasonable price for the tangible personal property.

(B) If the technology transfer agreement does not separately state a price for the tangible personal property, and the tangible personal property or like tangible personal property has been previously sold or leased, or offered for sale or lease, to third parties at a separate price, the price at which the tangible personal property was sold, leased, or offered to third parties shall be used to establish the retail fair market value of the tangible personal property subject to tax. The remaining amount charged under the technology transfer agreement is for the intangible personal property transferred.

(C) If the technology transfer agreement does not separately state a price for the tangible personal property, and the tangible personal property or like tangible personal property has not been previously sold or leased, or offered for sale or lease, to third parties at a separate price, the retail fair market value shall be equal to 200 percent of the cost of materials and labor used to produce the tangible personal property subject to tax. The remaining amount charged under the technology transfer agreement is for the intangible personal property transferred.

(D) For purposes of this paragraph, “technology transfer agreement” means any agreement under which a person who holds a patent or copyright interest assigns or licenses to another person the right to make and sell a product or to use a process that is subject to the patent or copyright interest.

(11) The amount of any tax imposed upon diesel fuel pursuant to Part 31 (commencing with Section 60001).

(12) (A) The amount of tax imposed by any Indian tribe within the State of California with respect to a retail sale of tangible personal property measured by a stated percentage of the sales or purchase price, whether the tax is imposed upon the retailer or the consumer.

(B) The exclusion authorized by subparagraph (A) shall only apply to those retailers who are in substantial compliance with this part.

For purposes of the sales tax, if the retailers establish to the satisfaction of the [Department] that the sales tax has been added to the total amount of the sale price and has not been absorbed by them, the total amount of the sale price shall be deemed to be the amount received exclusive of the tax imposed. Section 1656.1 of the Civil Code shall apply in determining whether or not the retailers have absorbed the sales tax.

Sales and Use Tax Annotations (Annotations)<sup>2</sup> 295.1242 (5/18/95), 295.1304 (7/3/96), 295.1319 (8/17/01), 295.1340 (2/20/96), 295.1410 (5/29/80), and 295.2000 (11/14/91) summarize the long-standing opinion of the Department's Legal Division that charges added to the price of tangible personal property to reimburse the retailer for a cost of doing business are included in gross receipts, unless expressly excluded or deductible from gross receipts pursuant to RTC section 6012. Also, Annotation 295.2000 summarizes the long-standing opinion of the Department's Legal Division that a fee a purchaser of tangible personal property is required to pay to reimburse the retailer for the cost of processing a credit card sale through the card issuer is included in gross receipts, as a nondeductible cost of doing business.

Annotation 295.1690 (8/16/78) summarize the long-standing opinion of the Department's Legal Division that "services that are part of the sale" within the meaning of subdivision (b)(1) of RTC section 6012 include any services the seller must perform to produce and sell tangible personal property, or for which the purchaser must pay as a condition of the purchase and/or functional use of the property. Also, Annotation 295.1502 (9/22/88) summarize the long-standing opinion of the Department's Legal Division that a retailer's charges for handling tangible personal property it sells are included in the retailer's gross receipts, as charges for services that are part of the sale.

Annotations 295.0647 (10/18/96), 295.0730 (10/4/76), 295.1675 (5/13/94) summarize the long-standing opinion of the Department's Legal Division that:

- Charges for services are included in the gross receipts from the sale of tangible personal property under RTC section 6012 when a purchaser must purchase the services to obtain the tangible personal property; and
- Charges for optional services, such as optional warranties, that are sold with tangible personal property, are not included in the gross receipts from the sale of the tangible personal property under RTC section 6012.

Also, the provisions regarding warranties in subdivision (b)(3) of California Code of Regulations (CCR), title 18, section (Regulation) 1546, Installing, Repairing, Reconditioning in General, incorporate that long-standing distinction between charges for mandatory and optional warranties.

In addition, Regulation 1628, Transportation Charges, currently clarifies when separately stated charges for transportation are excluded from "gross receipts" under subdivision (c)(7) of RTC section 6012, and not subject to sales or use tax. Subdivision (a) of Regulation 1628 clarifies when charges for transportation by a carrier are excluded from gross receipts and subdivision (b) of Regulation 1628 clarifies when charges for delivery by facilities of the retailer are excluded from gross receipts. Also, Annotation 557.0640 (12/2/64) summarizes the Legal Division's long-standing opinion that transportation by a retailer's employee is transportation by facilities of the retailer for purposes of applying subdivision (b) of Regulation 1628.

---

<sup>2</sup> "Annotations" are summaries of the conclusions reached in selected legal rulings of Department counsel. Annotations do not embellish or interpret the legal rulings of counsel which they summarize and do not have the force and effect of law. (Reg. 35101, subd. (a)(1).) However, they are entitled to a degree of deference in some situations. (*Yamaha Corp. of America v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 11-15.)

### *Proposition 64*

On November 8, 2016, California voters approved Proposition 64 (Prop. 64). As relevant here, Prop. 64 added the CTL to the RTC and imposed a marijuana excise tax, effective January 1, 2018. As added by Prop. 64, RTC section 34010 provided that “gross receipts” shall have the same meaning as set forth in RTC section 6012. Subdivision (a) of RTC section 34011 provided that “Effective January 1, 2018, a marijuana excise tax shall be imposed upon purchasers of marijuana or marijuana products sold in this state at the rate of 15 percent of the gross receipts of any retail sale by [specified retailers required to be licensed under specific provisions of the Business and Professions Code (BPC)].” Subdivision (b) of RTC section 34011 provided that “Except as otherwise provided by regulation, the tax levied under this section shall apply to the full price, if nonitemized, of any transaction involving both marijuana or marijuana products and any other otherwise distinct and identifiable goods or services, and the price of any goods or services, if a reduction in the price of marijuana or marijuana products is contingent on purchase of those goods or services.” Therefore, for purposes of the marijuana excise tax originally imposed by Prop. 64, taxable “gross receipts” included charges for marijuana or marijuana products and other goods or services under specified circumstances.

In addition, as added by Prop. 64, subdivision (c) of RTC section 34011 required the specified retailers to collect the marijuana excise tax from purchasers and remit it to the Department. RTC section 34015 also required the specified retailers to remit the marijuana excise taxes they were required to collect to the Department quarterly on or before the last day of the month following each quarterly period of three months with returns subject to audit by the Department. Subdivision (d) of RTC section 34011 provided that the marijuana excise tax was in addition to the sales and use tax imposed by the state and local governments. Also, subdivision (e) of RTC section 34011 provided that gross receipts include the marijuana excise tax for purposes of assessing sales and use tax. So, for example, if thirty dollars (\$30) was subject to marijuana excise tax, then a four dollar and fifty cent (\$4.50) marijuana excise tax would apply ( $\$30 \times .15$ ) and sales and use tax would apply to thirty-four dollars and fifty cents (\$34.50 or  $\$30 + \$4.50$ ).

### *Senate Bill No. 94*

In 2017, the Legislature enacted Senate Bill No. (SB) 94 (Stats. 2017, ch. 27). As relevant here, SB 94 replaced the references to “marijuana” with references to “cannabis” throughout the CTL. It replaced subdivision (b) of RTC section 34011 (quoted above), which clarified the meaning of gross receipts, with a new subdivision (b) that required a distributor that sold or transferred cannabis or cannabis products to a cannabis retailer to collect the cannabis excise tax from the cannabis retailer, sometimes before the cannabis or cannabis products were purchased from the cannabis retailer in a retail sale. It amended RTC section 34015 to require distributors to remit the cannabis excise taxes they were required to collect from cannabis retailers to the Department quarterly on or before the last day of the month following each quarterly period of three months with returns subject to audit by the Department. It also amended RTC section 34015 so that cannabis retailers were no longer required to remit cannabis excise tax to the Department or file returns subject to audit by the Department.

SB 94 also made it easier to calculate the amount of cannabis excise tax to be collected when a distributor sold or transferred cannabis or cannabis products to a cannabis retailer in an arm’s

length transaction. This was done by amending subdivision (a) of RTC section 34011 so that the cannabis excise tax was imposed upon purchasers of cannabis or cannabis products at a rate of 15 percent of the “average market price of any retail sale by a cannabis retailer.” This was also done by amending RTC section 34010 to define “average market price” to mean:

- The average retail price determined by the wholesale cost of the cannabis or cannabis products sold or transferred to a cannabis retailer, plus a mark-up, as determined by the Department, in an arm’s length transaction; and
- The cannabis retailer’s gross receipts from the retail sale of the cannabis or cannabis products in a nonarm’s length transaction.

Therefore, after the amendments made by SB 94, the amount of cannabis excise tax due on a retail sale of cannabis or cannabis products depended entirely on the retailer’s wholesale cost when the cannabis or cannabis products were sold or transferred to the retailer in an arm’s length transaction.

However, SB 94 did not make it easier for a distributor to calculate the amount of cannabis excise tax to be collected when a distributor sold or transferred cannabis or cannabis products to a cannabis retailer in a nonarm’s length transaction. This is because a cannabis retailer’s gross receipts from a retail sale of cannabis or cannabis products are indeterminable until the retail sale occurs. Also, SB 94 was silent about how a distributor was supposed to determine a retailer’s gross receipts from a subsequent retail sale, particularly when the sale had not occurred before the distributor was required to collect the cannabis excise tax on that sale from the cannabis retailer.

In addition, SB 94 renumbered subdivisions (d) and (e) of RTC section 34011 as subdivisions (c) and (d) without further amendments. Therefore, the cannabis excise tax was still in addition to the sales and use tax imposed by the state and local governments and gross receipts still included the cannabis excise tax for purposes of assessing sales and use tax. Also, SB 1289 (Stats. 2018, ch. 92) revised RTC section 34010 to provide that “gross receipts” has the same meaning as set forth in RTC section 6012, but it did not materially change the definition of gross receipts, as added by Prop. 64.

### *Regulation 3700*

The Department previously determined that there was an issue (or problem) regarding how the cannabis excise tax imposed by RTC section 34011, as amended by SB 94, applied to the sale of cannabis or cannabis products with cannabis accessories, such as vaping devices, which was not explicitly addressed in the CTL after SB 94 replaced subdivision (b) of RTC section 34011. The Department determined that the application of tax depended upon how the distributor sold or transferred the cannabis or cannabis products to the retailer, based upon the way SB 94 changed the imposition, collection, and remittance of cannabis excise tax. The Department also determined that the cost of cannabis accessories was included in the average market price to which the cannabis excise tax applied when a distributor sold or transferred cannabis or cannabis products to a cannabis retailer with cannabis accessories for a lump-sum charge. However, when a distributor separately stated the price of the cannabis or cannabis products from the cannabis

accessories, the cannabis excise tax applied to the average market price of the cannabis or cannabis products, and not to the separately stated charge for the cannabis accessories.

RTC section 34013 authorizes the Department to prescribe, adopt, and enforce regulations relating to the administration and enforcement of the CTL. In 2019, the Department adopted subdivisions (a)(2) and (i) of Regulation 3700, Cannabis Excise and Cultivation Tax, to clarify the meaning of the “average market price of any retail sale by a cannabis retailer,” as used in RTC section 34011, when a distributor sold or transferred cannabis or cannabis products to cannabis retailers with cannabis accessories. Subdivision (a)(2) provides that “cannabis accessories” has the same meaning as provided in Health and Safety Code (HSC) section 11018.2, which states that “cannabis accessories” means any equipment, products or materials of any kind which are used, intended for use, or designed for use in planting, propagating, cultivating, growing, harvesting, manufacturing, compounding, converting, producing, processing, preparing, testing, analyzing, packaging, repackaging, storing, smoking, vaporizing, or containing cannabis, or for ingesting, inhaling, or otherwise introducing cannabis or cannabis products into the human body. Subdivision (i) provides that the cost of cannabis accessories is included in the average market price to which the cannabis excise tax applied when a distributor sold or transferred cannabis or cannabis products to a cannabis retailer with cannabis accessories for a lump-sum charge. However, when a distributor separately stated the price of the cannabis or cannabis products from the cannabis accessories, the cannabis excise tax applied to the average market price of the cannabis or cannabis products, and not to the separately stated charge for the cannabis accessories. Regulation 3700 does not further clarify how a distributor is supposed to determine a cannabis retailer’s gross receipts from a retail sale in the case of a nonarm’s length transaction.

The Department also previously determined that the separately stated rule in subdivision (i) of Regulation 3700 did not ultimately ensure full compliance with RTC section 34011 as intended. This is because the cannabis excise tax is 15 percent. It is in addition to state and local sales and use tax. It is also included in gross receipts for purposes of assessing state and local sales and use tax. Therefore, some distributors and retailers misused the separately stated rule to evade the cannabis excise tax and gain a competitive advantage. They used the separately stated rule to artificially attribute taxable charges for cannabis or cannabis products to other tangible personal property, such as plastic bags and jars, for cannabis excise tax purposes.

### *AB 195*

On June 30, 2022, the Legislature enacted AB 195 (Stats. 2022, ch.56). As relevant here, AB 195 added RTC section 34011.2 and amended RTC sections 34011 and 34015 to:

- Change the cannabis excise tax so it is “imposed upon purchasers of cannabis or cannabis products sold in this state at 15 percent of the gross receipts of any retail sale by a cannabis retailer,” on and after January 1, 2023 (RTC, § 34011.2, subd. (a)).
- Remove the requirement for the distributor to collect the cannabis excise tax from the cannabis retailer on cannabis or cannabis products sold or transferred to the cannabis retailer on or after January 1, 2023.

- Require cannabis retailers to remit the cannabis excise tax imposed on and after January 1, 2023, directly to the Department with a return subject to audit by the Department. (RTC, §§ 34011.2, subd. (c), 34015).

However, the Legislature did not add a provision to the CTL to further clarify how the current cannabis excise tax applies to the retail sale of cannabis or cannabis products with other tangible personal property, such as packaging and vaping devices, on and after January 1, 2023.

Also, AB 195 amended subdivision (e) of RTC section 34013 to authorize the Department to prescribe, adopt, and enforce any emergency regulations, until January 1, 2024, as necessary to implement, administer, and enforce its duties under division 2 of the RTC, which includes the CTL and FCPL. Subdivision (e) also specifies that the emergency regulations adopted by the Department may remain in effect for two years from adoption.

#### *RTC sections 55061 and 55302*

Subdivision (a) of RTC section 34013 provides that the Department shall administer and collect the taxes imposed by the CTL pursuant to the FCPL. As relevant here, RTC section 55302 in the FCPL authorizes the Department to examine the books and records of any person liable for the payment of the cannabis excise taxes imposed by the CTL as it may deem necessary in carrying out the administration and collection of such taxes. Regulation 4901, Records, implements RTC section 55302. It requires a person liable for the payment of cannabis excise tax to maintain and make available for examination on request by the Department all records necessary to determine their correct cannabis excise tax liability and all records necessary for the proper completion of their cannabis excise tax returns. It also provides that those records include but are not limited to books of account, bills, receipts, invoices, cash register tapes, or other documents of original entry supporting the entries in the books of account, and the schedules or working papers used in connection with the preparation of their cannabis excise tax returns. Also, RTC section 55061 in the FCPL authorizes the Department to compute and determine the amount of cannabis excise tax to be paid under the CTL based upon any information available, and issue deficiency determinations (or billings) for the collection of unreported, underreported, or unpaid cannabis excise tax.

#### *Division 10*

Division 10 (commencing with section 26000) of the BPC defines “package” to mean any container or receptacle used for holding cannabis or cannabis products (BPC section 26001, subd. (ap)) and requires cannabis or cannabis products to be labeled and placed in a tamper-evident, child-resistant package, prior to delivery or sale at a cannabis retailer. (BPC section 26120, subd. (a).) The Department of Cannabis Control (DCC) has adopted regulations that further clarify that “package” or “packaging” means any container or wrapper that may be used for enclosing or containing any cannabis or cannabis product but does not include a shipping container or outer wrapping used solely for the transport of cannabis or cannabis products in bulk quantity to a licensed premises. (DCC Regulation 15000, subd. (yy).) DCC has also adopted regulations that further clarify division 10’s packaging requirements. (DCC Regulations 17401, 17411, and 17412.) Also, Annotation 295.1387 (11/15/91) summarizes the Legal Division’s long-standing opinion that amounts a purchaser of tangible personal property must pay to



compensate or reimburse a retailer for the cost of labor or materials used to package an item are generally included in taxable gross receipts under RTC section 6012.

### Emergency Regulation 3802

The Department previously determined that there was an issue (or problem within the meaning of GC section 11346.2, subd. (b)) because the CTL does not expressly clarify whether “the gross receipts of any retail sale by a cannabis retailer,” as used in RTC section 34011.2, include charges for other tangible personal property (non-cannabis items) purchased with cannabis or cannabis products in a retail sale. The Department previously determined that there were also issues (or problems) regarding whether cannabis retailers’ charges for services and transportation are included in their gross receipts for purposes of the cannabis excise tax imposed by RTC section 34011.2. The Department previously determined that the issues (or problems) were not addressed by subdivision (i) of Regulation 3700 because that subdivision clarifies the meaning of “the average market price of any retail sale by a cannabis retailer” as used in RTC section 34011 and the definition of “average market price” in RTC section 34010. The Department also previously determined that it was reasonably necessary to adopt emergency Regulation 3802, Gross Receipts from Sales of Cannabis and Cannabis Products, for the specific purpose of addressing the issues (or problems).

Emergency Regulation 3802 became operative on December 15, 2023. Also, emergency Regulation 3802 will be repealed by operation of law on December 16, 2025, unless the Department adopts it as permanent regulation through the regular rulemaking process in the Administrative Procedure Act (APA) (commencing with GC, § 11340) and submits the completed rulemaking file to the Office of Administrative Law (OAL) by December 15, 2025.

### *Charges for Non-Cannabis Items*

Subdivision (a) of RTC section 34011.2 only imposes cannabis excise tax on purchasers of cannabis or cannabis products. Also, subdivision (a) of RTC section 6012 provides that “gross receipts” mean the total amount of the sale price of the retail sales of retailers. Therefore, the Department determined that the gross receipts of any retail sale by a cannabis retailer, as used in subdivision (a) of RTC section 34011.2, include any amount the purchaser is required to pay to purchase cannabis or cannabis products.

The Department determined that whether the gross receipts of any retail sale by a cannabis retailer, as used in subdivision (a) of RTC section 34011.2, include charges for non-cannabis items, such as packaging, depends upon the terms of the retail sale of the cannabis or cannabis products because the tax applies to the gross receipts from that retail sale. The Department determined that when the cannabis retailer requires a purchaser to purchase specific non-cannabis items as a condition of the retail sale of cannabis or cannabis products, there is a bundled transaction. (*Bekkerman v. California Dept. of Tax & fee Administration* (2024) 99 Cap.App.5th 1264, 1269 (*Bekkerman*).) The Department also determined that when there is such a bundled transaction, the charges for the non-cannabis items included in the bundled transaction are required to be attributed to the cannabis or cannabis products and included in the cannabis retailer’s gross receipts from the sale of the cannabis or cannabis products. This is because:

- The charges are commingled in such a bundled transaction (*Bekkerman* at pp. 1273, 1274), regardless of whether the cannabis retailer segregates or separately states the charges;
- Including all the charges for such a bundled transaction in gross receipts is necessary to provide consistent tax treatment and certainty for cannabis retailers (*Bekkerman* at p. 1274); and
- Including all the charges for such a bundled transaction in gross receipts is necessary to discourage cannabis retailers from trying to evade the cannabis excise tax by artificially attributing commingled charges for cannabis or cannabis products to non-cannabis items included in such a bundled transaction. (*Levitt v. Faber et al.* (1937) 20 Cal.App.2d Supp. 758, 762 (*Levitt*).)

In addition, the Department determined that when a cannabis retailer does not require a purchaser to purchase specific non-cannabis items as a condition of the retail sale of cannabis or cannabis products, and a purchaser purchases the optional non-cannabis items with the cannabis or cannabis products it is not a bundled transaction. Also, when a transaction is not a bundled transaction, a reasonable amount charged for the optional non-cannabis items is not required to be attributed to the cannabis or cannabis products and included in the cannabis retailer's gross receipts from the sale of the cannabis or cannabis products. However, when the amount claimed as charged for optional non-cannabis items exceeds a reasonable amount, the excess amount is in fact charged for the cannabis or cannabis products. Therefore, the excess amount is required to be attributed to the cannabis or cannabis products and included in the cannabis retailer's gross receipts from the sale of the cannabis or cannabis products to discourage the cannabis retailer from trying to evade the cannabis excise tax by artificially attributing charges for cannabis or cannabis products to optional non-cannabis items. (*Levitt, supra*, at p. 762.)

#### *Charges for Services and Transportation*

Subdivision (b)(1) of RTC section 6012 requires charges for services that are part of the sale of tangible personal property to be included in gross receipts for sales tax purposes. Therefore, the Department determined that RTC section 6012 also requires charges for services that are part of the sale of cannabis or cannabis products to be included in gross receipts for purposes of the cannabis excise tax imposed by RTC section 34011.2.

Regulation 1628 currently clarifies when separately stated charges for transportation are excluded from "gross receipts" under subdivision (c)(7) of RTC section 6012. The Department also determined that the rules in Regulation 1628 should apply when determining if a cannabis retailer's charges for transportation are excluded from gross receipts for purposes of the cannabis excise tax imposed by RTC section 34011.2.

#### *Text of Emergency Regulation*

Based upon the above discussion, subdivision (a) of emergency Regulation 3802 clarifies that for purposes of the cannabis excise tax imposed by RTC section 34011.2 gross receipts from the retail sale of cannabis or cannabis products include any amount the purchaser is required to pay to purchase the cannabis or cannabis products, regardless of how the amount is denominated or

labeled on the invoice, receipt, or other document provided to the purchaser, unless the amount is excluded or deductible from gross receipts pursuant to RTC section 6012.

Subdivision (a) further clarifies that gross receipts specifically include, but are not limited to any amount the purchaser is required to pay for services that are part of the sale of the cannabis or cannabis products. For example, when a cannabis retailer requires a purchaser to pay a fee to reimburse itself for the cost of processing the purchaser's credit card payment for the purchase of cannabis, the fee is included in the gross receipts from the sale of the cannabis.

Subdivision (a) also further clarifies that gross receipts specifically include, but are not limited to any amount the purchaser is required to pay for tangible personal property, including packaging, the purchaser is required to purchase as condition of the sale of the cannabis or cannabis products. For example, if a purchaser is required to purchase a plastic bag or jar as a condition of the retail sale of the cannabis, the amount the purchaser is required to pay for the plastic bag or jar is included in the gross receipts from the sale of the cannabis. If a purchaser is required to purchase a cartridge as a condition of the retail sale of the cannabis product contained in the cartridge, the amount the purchaser is required to pay for the cartridge is included in the gross receipts from the sale of the cannabis product. Also, if a purchaser is required to purchase a cartridge and vaping device as a condition of the retail sale of the cannabis product contained in the cartridge, the amount the purchaser is required to pay for the cartridge and vaping device is included in the gross receipts from the sale of the cannabis product.

Subdivision (b)(1) of emergency Regulation 3802 clarifies that, for purposes of the cannabis excise tax, gross receipts from the retail sale of cannabis or cannabis products does not include a reasonable amount charged for optional tangible personal property purchased with cannabis or cannabis products in the same retail sale regardless of whether those amounts are separately stated on the invoice, receipt, or other document provided by the cannabis retailer to the purchaser and regardless of whether the optional tangible personal property is purchased with the cannabis or cannabis products as a unit. Subdivision (b)(1)(A) clarifies that "optional tangible personal property" means tangible personal property that a purchaser is not required to purchase as a condition of the sale of the cannabis or cannabis product because the purchaser could purchase that cannabis or cannabis product or the same kind of cannabis or cannabis product, as defined in subdivision (b)(1)(B), from the cannabis retailer without purchasing the tangible personal property. Subdivision (b)(1)(B) further provides that for purposes of subdivision (b)(1)(A), "same kind of cannabis" means cannabis that is the same brand, quantity, strain, and type (e.g., flower, pre-roll, shake) as the cannabis purchased and "same kind of cannabis product" means cannabis product that is the same brand, quantity, strain, and type (e.g., beverage, capsule, concentrate, edible, tincture, topical, cannabis oil) as the cannabis product purchased.

Subdivision (b)(1)(C) of emergency Regulation 3802 provides examples to further illustrate these points and clarify that emergency Regulation 3802 does not generally include all charges for tangible personal property, other than cannabis or cannabis products, in gross receipts subject to the cannabis excise tax. The subdivision provides that when a cannabis retailer sells seven-gram jars of XYZ brand Hawaiian Punch strain cannabis flower separately from lighters or pipes so that purchasers are not required to purchase the lighters or pipes as a condition of the sale of the cannabis, then a lighter or pipe is optional tangible personal property when a purchaser

chooses to purchase one with a seven-gram jar of XYZ brand Hawaiian Punch strain cannabis flower in the same retail sale. Also, when a cannabis retailer sells one-gram cartridges of XYZ brand Hawaiian Punch strain cannabis oil separately from vaping devices so that purchasers are not required to purchase the vaping devices as a condition of the sale of the cannabis products, then a vaping device is optional tangible personal property when a purchaser chooses to purchase one with a one-gram cartridge of XYZ brand Hawaiian Punch strain cannabis oil in the same retail sale.

Subdivision (b)(2) of emergency Regulation 3802 clarifies that the cannabis retailer has the burden to maintain and make available to the Department records that establish that tangible personal property purchased with cannabis or cannabis products in a retail sale was optional tangible personal property. If the Department determines that tangible personal property purchased with cannabis or cannabis products in a retail sale was not optional tangible personal property, the entire amount charged for the tangible personal property shall be included in the gross receipts from the retail sale of the cannabis or cannabis products pursuant to subdivision (a).

Subdivision (b)(3) of emergency Regulation 3802 clarifies that the cannabis retailer also has the burden to maintain and make available to the Department records that establish that the amount charged for optional tangible personal property purchased with cannabis or cannabis products in a retail sale was reasonable. If the Department determines that any amount charged for optional tangible personal property exceeds a reasonable charge, the excess amount shall be included in the gross receipts from the sale of the cannabis or cannabis products pursuant to subdivision (a). The factors the Department may consider in determining whether the amount charged for optional tangible personal property is reasonable, include, but are not limited to:

(A) The wholesale cost of optional tangible personal property.

(B) The size of the markup added to the wholesale cost of the optional tangible personal property.

(C) The amount charged for the cannabis or cannabis products sold with the optional tangible personal property in the same retail sale.

Finally, subdivision (c) of emergency Regulation 3802 clarifies that for purposes of the cannabis excise tax, gross receipts from the retail sale of cannabis or cannabis products excludes certain transportation charges as provided in RTC section 6012 and Regulation 1628, Transportation Charges.

#### Proposed Adoption of Emergency Regulation 3802 with Proposed Amendments

The Department subsequently determined that there is an issue (or problem) because subdivision (a)(1) of emergency Regulation 3802 clarifies that gross receipts specifically include, but are not limited to any amount the purchaser is required to pay for services that are part of the sale of the cannabis or cannabis products. However, the Department inadvertently included an example in subdivision (a)(1) of an amount included in gross receipts because the purchaser is required to pay it to reimburse the cannabis retailer for a cost of doing business, rather than an example of an amount included in gross receipts because the purchaser is required to pay it for a service that is

part of the sale of cannabis, as intended. The Department also determined that there is an issue (or problem) because emergency Regulation 3802 does not expressly clarify that for purposes of the cannabis excise tax imposed by RTC section 34011.2 gross receipts from the sale of cannabis or cannabis products includes any amount a purchaser is required to pay to reimburse the cannabis retailer for the cost of doing business, even though subdivision (a)(1) includes an example of such an amount. Therefore, the Department determined that it is reasonably necessary to propose to amend subdivision (a) of emergency Regulation 3802 for the specific purpose of addressing both issues (or problems).

The proposed amendments delete “for” from the end of subdivision (a) of emergency Regulation 3802 for solely grammatical reasons. The proposed amendments replace the first sentence in subdivision (a)(1) with a new sentence that is consistent with the example in subdivision (a)(1) and expressly clarifies that for purposes of the cannabis excise tax imposed by RTC section 34011.2, gross receipts from the sale of cannabis or cannabis products include any amount a purchaser is required to pay “To reimburse the cannabis retailer for the cost of doing business, including the costs of the sale.” The proposed amendments also add a new subdivision (a)(2) to expressly clarify that for purposes of the cannabis excise tax imposed by RTC section 34011.2 gross receipts from the sale of cannabis or cannabis products include any amount a purchaser is required to pay “For services that are part of the sale of the cannabis or cannabis products. For example, when a cannabis retailer requires a purchaser to pay a handling charge for services provided during their purchase of cannabis, the service charge is included in the gross receipts from the sale of the cannabis.” The amendments also renumber current subdivision (a)(2), as subdivision (a)(3) and add “For” to the beginning of renumbered subdivision (a)(3) for grammatical reasons.

The Department determined that there is an issue (or problem) with emergency Regulation 3802 because the second and third sentences in subdivision (b)(3) refer to the “amount charged for optional tangible personal property.” However, those sentences are about determining whether any of the amount claimed as charged for optional tangible personal property is in fact charged for cannabis or cannabis products and is required to be included in the cannabis retailer’s gross receipts for purposes of the cannabis excise tax imposed by RTC section 34011.2. Therefore, the Department determined that it is reasonably necessary to propose non-substantive amendments to clarify that both sentences are referring to “the amount claimed as charged for optional tangible personal property” for the specific purposes of addressing the issue (or problem).

The Department also determined that there is an issue (or problem) with emergency Regulation 3802 because it may be necessary for the Department to consider factors affecting the value of the optional tangible personal property or the cannabis or cannabis products sold with the optional tangible personal property, such as scarcity, to determine whether the amount claimed as charged for optional tangible personal property is reasonable in some cases. However, subdivision (b)(3) does not expressly refer to such factors. Therefore, the Department determined that it is reasonably necessary to propose to amend subdivision (b)(3) to expressly clarify that the Department may consider any factors affecting the value of the optional tangible personal property or the cannabis or cannabis products sold with the optional tangible personal property in same retail sale, such as scarcity, in determining whether the amount claimed as charged for optional tangible personal property is reasonable for the specific purposes of addressing the issue (or problem).

Also, for the reasons discussed above, the Department determined that it is reasonably necessary to propose to adopt emergency Regulation 3802 with the proposed amendments through the APA's regular rulemaking process for the specific purposes of addressing the issues (or problems) regarding charges for non-cannabis items, charges for services and transportation, and charges to reimburse the cannabis retailer for the cost of doing business discussed above. The Department anticipates that the adoption of emergency Regulation 3802 with the proposed amendments through the APA's regular rulemaking process will promote fairness and benefit cannabis retailers, purchasers, and the Department by clarifying the application of the cannabis excise tax. In addition, the Department has determined that the adoption of emergency Regulation 3802 with the proposed amendments is not mandated by federal law or regulations, and there are no federal regulations or statutes that are identical to emergency Regulation 3802 or the proposed amendments to emergency Regulation 3802.

#### DOCUMENTS RELIED UPON

The Department relied upon Department staff's understanding of the CTL and SUTL in proposing to adopt emergency Regulation 3802 with the proposed amendments. The Department did not rely upon any technical, theoretical, or empirical study, report or similar document.

#### ALTERNATIVES CONSIDERED

The Department considered whether to begin the APA's regular rulemaking process to adopt emergency Regulation 3802 with the proposed amendments at this time or, alternatively, whether to take no action at this time. The Department decided to begin the APA's regular rulemaking process to adopt emergency Regulation 3802 with the proposed amendments because the Department determined that the adoption of emergency Regulation 3802 with the proposed amendments is reasonably necessary for the reasons set forth above.

The Department also considered whether to extend the provisions of subdivision (i) of Regulation 3700 so that they apply to the cannabis excise tax imposed by RTC section 34011.2 or adopt a similar separately stated rule to address the issues (or problems) regarding the cannabis excise tax imposed by RTC section 34011.2. The Department determined that the provisions of subdivision (i) of Regulation 3700 are inconsistent with RTC section 34011.2 because:

- RTC section 34011.2 does not require distributors to collect cannabis excise tax and the transaction in which a distributor sells or transfers cannabis or cannabis products to the cannabis retailer is not relevant to the imposition, collection, remittance, or reporting of the current cannabis excise tax;
- The CTL, including RTC section 34011.2, does not require charges for cannabis, cannabis products, or non-cannabis items sold with cannabis or cannabis products to be separately stated (see *Dell, Inc. v. Superior Court* (2008) 159 Cal.App.4th 911, 917, 929, 931); and
- The CTL does not refer to cannabis accessories or require charges for cannabis accessories to be excluded from "the gross receipts of any retail sale by a cannabis retailer" for purposes of the cannabis excise tax imposed by RTC section 34011.2.

The Department determined that the separately stated rule in subdivision (i) of Regulation 3700 did not ensure full compliance with RTC section 34011 as intended because some distributors and retailers misused the separately stated rule to evade the cannabis excise tax and gain a competitive advantage. The Department also determined that a separately stated rule would not ensure full compliance with RTC section 34011.2 for similar reasons. Therefore, the Department determined that it would be unreasonable to use subdivision (i) of Regulation 3700 or a similar separately stated rule to address the issues (or problems) regarding the cannabis excise tax imposed by RTC section 34011.2 discussed above and rejected that alternative as unreasonable.

The Department did not reject any reasonable alternative to the adoption of emergency Regulation 3802 with the proposed amendments, including any reasonable alternative 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 to the adoption of emergency Regulation 3802 with the proposed amendments has been identified and brought to the Department'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 GC SECTION 11346.2, SUBDIVISION (b)(5) AND ECONOMIC IMPACT ASSESSMENT REQUIRED BY GC SECTION 11346.3, SUBDIVISION (b)

The Department assessed the economic impact of adopting emergency Regulation 3802 with the proposed amendments on California businesses and individuals. The Department determined that cannabis retailers are the only persons required to comply with emergency Regulation 3802 and that the adoption of emergency Regulation 3802 with the proposed amendments will only impact cannabis retailers.

The Department determined that cannabis retailers were required to begin complying with emergency Regulation 3802 when it became operative on December 15, 2023, and that they should currently be complying with its provisions. The Department also determined that cannabis retailers will not incur any costs to comply with the provisions of emergency Regulation 3802 with the proposed amendments that they would not otherwise incur to comply with the current provisions of emergency Regulation 3802. Therefore, the Department determined that the adoption of emergency Regulation 3802 with the proposed amendments will not impose additional compliance costs on cannabis retailers.

In addition, the Department reviewed the information reported by registered cannabis retailers on their cannabis excise tax and sales and use tax returns filed for the first three quarters of 2023, which were due before emergency Regulation 3802 became operative (pre-emergency regulation period), and the fourth quarter of 2023 and first two quarters of 2024, which were due after emergency Regulation 3802 became operative (post-emergency regulation period). After adjusting the information reported on the sales and use tax returns for the inclusion of cannabis excise tax in gross receipts for sales tax purposes, the Department determined that 44.72 percent

of the returns filed by the registered cannabis retailers did not report any non-cannabis sales during both periods. The Department determined that the registered cannabis retailers reported that on average only 1.13 percent of their gross receipts for sales tax purposes were from sales of non-cannabis items during the pre-emergency regulation period. The Department determined that the registered cannabis retailers reported that on average only 2.68 percent of their gross receipts for sales tax purposes were from sales of non-cannabis items during the post-emergency regulation period. The Department also determined that there were some registered cannabis retailers that reported that more than 50 percent of their gross receipts for sales tax purposes were from sales of non-cannabis items during both periods after adjusting the information reported for the inclusion of cannabis excise tax in gross receipts for sales tax purposes.

Based on the return information, the Department determined that the registered cannabis retailers who reported that more than 50 percent of their gross receipts for sales tax purposes were from sales of non-cannabis items were probably non-compliant cannabis retailers that were artificially attributing charges for cannabis or cannabis products to non-cannabis items. This is because there was such a substantial difference in the amounts they reported when compared to the amounts reported by the registered cannabis retailers as a group. The Department determined that the sales of non-cannabis items reported by the non-compliant cannabis retailers were also probably artificially increasing the average percent of gross receipts from sales of non-cannabis items reported by the registered cannabis retailers as a group, and that the average percent of gross receipts from sales of non-cannabis items for the pre- and post-emergency regulation periods were probably less than 1.13 and 2.68 percent, respectively. Therefore, the Department determined that sales of non-cannabis items represent a small portion of most compliant cannabis retailers' total sales. The Department also determined that the provisions of emergency Regulation 3802 that clarify whether gross receipts for cannabis excise tax purposes include charges for non-cannabis items purchased with cannabis or cannabis products in a retail sale will not have a material impact on compliant cannabis retailers. This is because the clarifications relate to a small portion of their total sales and clarify that gross receipts for cannabis excise tax purposes do not include a reasonable amount charged for optional non-cannabis items.

As a result, the Department determined that the proposed regulatory action is not a major regulation, as defined in GC section 11342.548 and CCR, title 1, section 2000. The Department also prepared the economic impact assessment required by GC section 11346.3, subdivision (b)(1), and the Department determined in the economic impact assessment that the adoption of emergency Regulation 3802 with the proposed amendments will neither create nor eliminate jobs in the State of California nor result in the creation of new businesses or the elimination of existing businesses within the State of California and will not affect the expansion of businesses currently doing business within the State of California.

Furthermore, emergency Regulation 3802 with the proposed amendments does not regulate the health and welfare of California residents, worker safety, or the state's environment. Therefore, the Department determined that the adoption of emergency Regulation 3802 with the proposed amendments will not affect the benefits of the regulation 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 Department's initial determination that the adoption of emergency Regulation 3802 with the proposed amendments will not have a significant adverse economic impact on business.