

**Notice of Proposed Emergency Action and Finding of Emergency**

**The California Department of Tax and Fee Administration**

**Has Adopted California Code of Regulations, Title 18, Section 3802,**

**Gross Receipts from Sales of Cannabis and Cannabis Products**

NOTICE IS HEREBY GIVEN that the California Department of Tax and Fee Administration (Department), pursuant to the authority vested in the Department pursuant to Revenue and Taxation Code (RTC) section 34013, has adopted California Code of Regulations, title 18, section (Regulation or Reg.) 3802, Gross Receipts from Sales of Cannabis and Cannabis Products, as an emergency regulation in accordance with the Administrative Procedure Act (APA) (Gov. Code (GC), § 11340 et seq.). Emergency Regulation 3802 clarifies the meaning of the phrase “gross receipts of any retail sale by a cannabis retailer” as used in subdivision (a)(1) of RTC section 34011.2.

**FINDING OF EMERGENCY**

*Section 48 Statement*

Subdivision (a) of GC section 11346.1 requires that, at least five working days prior to submission of the proposed emergency regulation to the Office of Administrative Law (OAL), the Department provide a notice of the proposed emergency action to every person that has filed a request for notice of regulatory action with the Department. Subdivision (b) of GC section 11349.6 provides that after submission of the proposed emergency regulation to OAL, OAL shall allow interested persons five calendar days to submit comments on the proposed emergency regulation.

*Statement of Emergency*

Subdivision (c) of RTC section 34013 generally authorizes the Department to prescribe, adopt, and enforce regulations relating to the administration and enforcement of the Cannabis Tax Law (CTL) (RTC, § 34010 et seq.), including, but not limited to, collections, reporting, refunds, and appeals. Subdivision (e) of RTC section 34013, as amended by Assembly Bill No. (AB) 195 (Stats. 2022, ch. 56), authorizes the Department to prescribe, adopt, and enforce any emergency regulations as necessary to implement, administer, and enforce its duties under the CTL until January 1, 2024. Subdivision (e) also provides that any emergency regulation prescribed, adopted, or enforced pursuant to RTC section 34013 shall be adopted in accordance with the APA, and, for purposes of the APA, including GC section 11349.6, the adoption of the regulation is an emergency and shall be considered by OAL as necessary for the immediate preservation of the public peace, health and safety, and general welfare. Notwithstanding any other law, the emergency regulations adopted by the Department may remain in effect for two years from adoption and may be readopted in accordance with subdivision (h) of GC section 11346.1.

**AUTHORITY**

RTC section 34013.

## REFERENCE

RTC sections 6012, 34010, 34011.2, 55061, and 55302

## INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

### Summary of Existing Laws and Regulations

#### *Sales and Use 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. (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.

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<sup>1</sup> The administration of the Sales and Use Tax Law (SUTL) (RTC, § 6001 et seq.), CTL, and Fee Collection Procedures Law (FCPL) was transferred from the State Board of Equalization (Board) to the Department, operative July 1, 2017, by AB 102 (Stats. 2017, ch. 16) and references to the "Board" in the SUTL, CTL, and FCPL statutes discussed in this notice mean the "Department" pursuant to 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> 295.0647 (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 Regulation 1546, Installing, Repairing, Reconditioning in General, incorporate that long-standing distinction between charges for mandatory and optional warranties.

Annotation 295.1187 (12/13/95) summarizes the Legal Division's long-standing opinion that local and district sales and use taxes imposed in accordance with the Bradley-Burns Uniform Local Sales and Use Tax Law (commencing with RTC section 7200) or Transactions and Use Tax Law (commencing with RTC section 7251) are excluded from gross receipts under subdivisions (c)(5) and (6) of RTC section 6012. However, amounts a purchaser of tangible personal property must pay to compensate or reimburse a retailer for other taxes imposed on the retailer by a city, county, city and county, or rapid transit district, including, but not limited to, business taxes measured by a business's gross receipts, are not excluded from gross receipts under subdivisions (c)(5) and (6) of RTC section 6012. This is because the Legal Division's opinion is that local taxes are only imposed "upon or with respect to retail sales of tangible

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<sup>2</sup> "Annotations" are summaries of the conclusions reached in selected legal rulings of 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).)

personal property measured by a stated percentage of sales price or gross receipts,” under subdivision (c)(5), if they are imposed on individual retail sales of tangible personal property and expressly measured by a stated percentage of “sales price” or “gross receipts,” as defined in RTC sections 6011 and 6012, respectively.

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.

#### *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” has 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.

Also, 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.

#### *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.

### *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.

The Department also adopted subdivisions (a)(2) and (i) of Regulation 3700, Cannabis Excise and Cultivation Tax, in 2019 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) clarifies how the cannabis excise tax imposed by RTC section 34011 applied when a distributor sold or transferred cannabis or cannabis products to cannabis retailers with cannabis accessories. It 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.

#### *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 cannabis accessories, such as vaping devices, on and after January 1, 2023.

#### *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, as incorporated into the CTL by subdivision (a) of RTC section 34013, authorizes the Department to examine the books and records of any person liable for the payment of the cannabis excise taxes imposed by RTC section 34011 or 34011.2 as it may deem necessary in carrying out the administration and collection of such taxes. Also, RTC section 55061 in the FCPL authorizes the Department to compute and determine the amount of cannabis excise tax to be paid under RTC section 34011 and 34011.2, based upon any information available, and issue deficiency determinations (or billing) 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.

## Effect, Objective, and Benefits of Emergency Regulation 3802

### *Issues and Draft Emergency Regulation*

The Department determined that there is now an issue (or problem) regarding how the cannabis excise tax imposed by RTC section 34011.2 applies to charges for other tangible personal property purchased with cannabis or cannabis products in a retail sale, which is not explicitly addressed in the CTL or subdivision (i) of Regulation 3700, which clarifies the application of the cannabis excise tax imposed by RTC section 34011, not the cannabis excise tax imposed by RTC section 34011.2. The Department also determined that the provisions of subdivision (i) of Regulation 3700 are not consistent with RTC section 34011.2 because that section 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 retailer is not relevant to the imposition, collection, remittance, or reporting of the current cannabis excise tax. This is also because RTC section 34011.2 does not require charges for cannabis, cannabis products, or other tangible personal property sold with cannabis or cannabis products to be separately stated.

The Department determined that whether the cannabis excise tax imposed by RTC section 34011.2 applies to charges for other tangible personal property sold with cannabis or cannabis products depends upon how the cannabis retailer sold the cannabis or cannabis products to the purchaser in the taxable retail sale, based upon subdivision (a) of RTC section 34011.2, which makes the “gross receipts of any retail sale by a cannabis retailer” the measure of the tax. The Department also determined that when a cannabis retailer requires a purchaser to purchase specific tangible personal property as a condition of the retail sale of cannabis or cannabis products, then the charges for the tangible personal property are included in the cannabis retailer’s gross receipts from the sale of the cannabis or cannabis products, subject to cannabis excise tax, under subdivision (a) of RTC section 34011.2. However, when a cannabis retailer does not require a purchaser to purchase specific tangible personal property as a condition of the retail sale of cannabis or cannabis products, then when a purchaser purchases that tangible personal property with the cannabis or cannabis products the amount charged for that optional tangible personal property is not included in the cannabis retailer’s gross receipts from the sale of the cannabis or cannabis products, subject to cannabis excise tax, under subdivision (a) of RTC section 34011.2.

In addition, the Department determined that there is now an issue (or problem) because some cannabis retailers are confused about whether subdivision (i) of Regulation 3700 somehow applies when determining whether their charges for cannabis accessories, including packaging, are included in their gross receipts for purposes of the cannabis excise tax imposed by RTC section 34011.2. The Department also determined that there may be issues (or problems) regarding whether cannabis retailers’ charges for services, taxes, and transportation are included in their gross receipts for purposes of the cannabis excise tax imposed by RTC section 34011.2. Therefore, the Department determined that it was reasonably necessary to prepare a draft of emergency Regulation 3802 to have the effect and accomplish the objective of addressing all

those issues (or problems).

As relevant here, subdivision (a) of the draft emergency regulation incorporated the definition of “gross receipts” from RTC section 6012 by providing that “‘Gross receipts’ from the sale of cannabis or cannabis products for purposes of the cannabis excise tax imposed by Revenue and Taxation Code (RTC) section 34011.2 (cannabis excise tax) has the same meaning as ‘gross receipts’ from the sale of tangible personal property as set forth in RTC section 6012.”

Subdivision (a) also provided that, in general, and as specifically clarified in the regulation, gross receipts for purposes of the cannabis excise tax include amounts that are included in gross receipts under RTC section 6012 for sales and use tax purposes, amounts that are not deductible from gross receipts under RTC section 6012 for sales and use taxes purposes are not deductible from gross receipts for cannabis excise tax purposes, and amounts excluded from gross receipts under RTC section 6012 for sales and use taxes purposes are excluded from gross receipts for cannabis excise tax purposes.

Subdivision (b) of the draft emergency regulation clarified that, for purposes of the cannabis excise tax, the “total amount of the sale price,” as used in RTC section 6012, includes any amount the purchaser is required to pay to purchase cannabis or cannabis products, regardless of how the amount is denominated or labeled on the invoice, receipt, or other document provided to the purchaser. It also clarified that the “total amount of the sale price,” specifically includes any amount the purchaser is required to pay for any of the following:

- (1) Services that are incidental to or part of the sale of the cannabis or cannabis products, including, but not limited to, service and convenience charges or fees.
- (2) Taxes imposed by any city, county, city and county, or rapid transit district on the sale of the cannabis or cannabis products, except as provided in subdivision (c).
- (3) Transportation of the cannabis or cannabis products, including, but not limited to, delivery charges or fees, except as provided in subdivision (d).
- (4) Packaging, except as provided in subdivision (e).
- (5) Tangible personal property other than packaging sold with the cannabis or cannabis products as a unit or for a lump sum price, except as provided in subdivision (e).

Subdivision (c) of the draft emergency regulation clarified that, for purposes of the cannabis excise tax, the “total amount of the sale price,” as used in RTC section 6012, does not include local taxes imposed in accordance with the Bradley-Burns Uniform Local Sales and Use Tax Law (commencing with RTC section 7200) or Transactions and Use Tax Law (commencing with RTC section 7251). However, other amounts a purchaser of cannabis or cannabis products must pay to compensate or reimburse a cannabis retailer for taxes imposed on the cannabis retailer by a city, county, city and county, or rapid transit district, including, but not limited to, cannabis business taxes measured by a cannabis retailer’s gross receipts, are not excluded from the sale price charged for cannabis or cannabis products to make the regulation consistent with Annotation 295.1187.

Subdivision (d) of the draft emergency regulation clarified that, for purposes of the cannabis excise tax, the “total amount of the sale price,” as used in RTC section 6012, does not include charges for transportation that are not subject to sales and use tax, as provided in Regulation

1628. It clarified that transportation by the retailer's employee is "transportation by facilities of the retailer" for purposes of Regulation 1628 to make the regulation consistent with Annotation 557.0640. It also clarified that charges a purchaser of cannabis or cannabis products must pay a cannabis retailer for delivery by facilities of the retailer are taxable, unless they satisfy the requirements of subdivision (b)(2) of Regulation 1628.

Subdivision (e) of the draft emergency regulation clarified that, for purposes of the cannabis excise tax, the "total amount of the sale price," as used in RTC section 6012, does not include a reasonable amount charged for optional packaging or other optional tangible personal property sold with cannabis or cannabis products as a unit or for a lump sum price in a 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. Subdivision (e) included separate provisions explaining when packing and other tangible personal property sold with cannabis or cannabis products are optional because cannabis and cannabis products cannot be legally sold at retail in this state, unless they are in packaging that satisfies the BPC requirements discussed above. Subdivision (e) established a rebuttable presumption that that packaging and other tangible personal property sold with cannabis or cannabis products as a unit or for a lump sum price are not optional. Subdivision (e) clarified that it is the cannabis retailer's burden to maintain and make available records to establish that packing or other tangible personal property sold with cannabis or cannabis products is optional. Subdivision (e) also clarified that it is the cannabis retailer's burden to maintain and make available records to establish that the amount charged for optional packaging and other optional tangible person property is reasonable to prevent retailers from shifting prices to avoid cannabis excise tax.

### *Interested Parties Comments*

The Department distributed the draft of emergency Regulation 3802 to the interested parties with a Discussion Paper dated October 2, 2023. The Department also conducted an interested parties meeting on October 12, 2023, to discuss the draft emergency regulation and accepted written comments.

In their oral and written comments, some interested parties raised a general concern that the draft emergency regulation may go beyond what Prop. 64 allows in terms of taxation. Some interested parties also said they thought the way subdivision (a) of the draft emergency regulation incorporated RTC section 6012 expanded the base of the cannabis excise tax imposed by RTC section 34011.2 beyond cannabis and cannabis products to include items that are generally subject to sales and use tax.

Some interested parties agreed with the part of subdivision (b) of the draft emergency regulation, which provided that the measure of the cannabis excise tax imposed by RTC section 34011.2 includes any amount the purchaser is required to pay to purchase cannabis or cannabis products. They also agreed with the part of subdivision (b)(1), which provided that charges for "services that . . . are part of the sale of the cannabis or cannabis products" are included in the measure of the cannabis excise tax imposed by RTC section 34011.2. However, they also said that the provisions of subdivision (b)(1), which provided that the measure of the cannabis excise tax includes charges for "services that are incidental to . . . the sale of the cannabis or cannabis

products, including, but not limited to, service and convenience charges or fees,” were unclear and should be deleted or further clarified to avoid taxing charges for nontaxable services.

Some interested parties disagreed with the provisions of subdivisions (b)(2) and (c) of the draft emergency regulation, which incorporated the Legal Division’s opinion regarding the meaning of subdivisions (c)(5) and (6) of RTC section 6012. They said they thought the provisions were inconsistent with subdivision (c)(5) of RTC section 6012, which refers to “any tax.” They also said they thought the Department lacked the authority to adopt the provisions of subdivisions (b)(2) and (c) of the draft emergency regulation under RTC section 34013 because they fall within the realm of the SUTL.

Some interested parties said that subdivisions (b)(3) and (d) of the draft emergency regulation were unnecessary because there is no confusion in the cannabis industry regarding the treatment of transportation charges. Also, some interested parties disagreed with the way subdivisions (b)(3) and (d) were written. They said that subdivision (c)(7) of RTC section 6012 provides an exclusion from gross receipts for specified transportation charges and that the emergency regulation should be rewritten so that it explains when transportation charges are excluded from gross receipts.

Most of the interested parties disagreed with subdivisions (b)(4) and (5) and (e) of the draft emergency regulation because those subdivisions expanded the base of the cannabis excise tax imposed by RTC section 34011.2 beyond cannabis and cannabis products. Some interested parties said they interpreted RTC section 34011.2, subdivision (i) of Regulation 3700, and the definitions of “cannabis,” “cannabis products,” and “cannabis accessories” in HSC sections 11018, 11018.1, and 11018.2 as excluding charges for cannabis accessories from the cannabis excise tax. Some interested parties said they did not think there is a sufficient distinction between RTC sections 34011 and 34011.2 to support including charges for cannabis accessories in gross receipts subject to the cannabis excise tax imposed by RTC section 34011.2. Some interested parties said that Annotations 295.0647, 295.0730, 295.1675 did not support the optional requirement in subdivision (e) because the Annotations relate to services, and that the emergency regulation should not include a requirement that tangible personal property sold with cannabis or cannabis products be optional. Some interested parties said that the BPC’s packaging requirements make it impossible for a cannabis retailer to legally comply with the optional packaging requirement in subdivision (e). Also, some of the interested parties’ comments indirectly indicated that they were having some difficulty understanding the optional requirements in subdivision (e).

### *Changes to the Emergency Regulation*

The Department reconsidered the provisions included in the draft emergency regulation in response to the issues raised by the interested parties’ comments. The Department also determined that it was necessary to revise emergency Regulation 3802 to address some of the issues raised by the interested parties and generally clarify how the optional requirement applies to other tangible personal property sold with cannabis or cannabis products in a retail sale.

The Department intended for subdivision (a) of the draft emergency regulation to generally incorporate the definition of “gross receipts” from RTC section 6012 and establish general rules for applying that definition to gross receipts from retail sales by cannabis retailers. The Department did not intend for subdivision (a) of the draft emergency regulation to expand the base of the cannabis excise tax imposed by RTC section 34011.2 to generally include all gross receipts from sales of tangible personal property subject to sales and use tax, but the Department understands that some interested parties did read it that way. Also, the definition of “gross receipts” from RTC section 6012 is already incorporated into the CTL by RTC section 34010. Therefore, the Department determined that it was not necessary to expressly incorporate the definition of “gross receipts” from RTC section 6012 into emergency Regulation 3802, at this time, because it is already incorporated into the CTL.

In addition, to avoid any unnecessary confusion, the Department deleted draft subdivision (a) from emergency Regulation 3802. The Department revised and reformatted the provisions of draft subdivisions (b) and (b)(1) that some interested parties agreed with, as new subdivisions (a) and (a)(1) of emergency Regulation 3802. The Department also added provisions to new subdivision (a) to clarify that gross receipts do not include amounts that are excluded or deductible from gross receipts pursuant to RTC section 6012 or a regulation implementing that section to ensure that reformatted subdivision (a) is not overly broad. Revised and reformatted subdivisions (a) and (a)(1) now clarify that:

(a) For purposes of the cannabis excise tax imposed by Revenue and Taxation Code (RTC) section 34011.2 (cannabis excise tax) “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 or a regulation implementing that section. “Gross receipts” specifically include, but are not limited to, any amount the purchaser is required to pay for: (1) Services that are part of the sale of the cannabis or cannabis products.

Annotation 295.1187 summarizes and provides notice of the Legal Division’s long-standing opinion regarding the meaning of the local tax provisions in subdivisions (c)(5) and (6) of RTC section 6012. The Department intended for subdivisions (b)(2) and (c) of the draft emergency regulation to incorporate and provide additional notice to cannabis retailers about the Legal Division’s long-standing opinion. However, there is a possibility that subdivisions (b)(2) and (c) of the draft emergency regulation could be read as implementing subdivisions (c)(5) and (6) of RTC section 6012 for sales and use tax purposes, and the Department does not have authority under RTC section 34013 to adopt emergency regulations relating to the SUTL. The Department also determined that it is not necessary to incorporate the Legal Division’s long-standing opinion into emergency Regulation 3802 at this time because Annotation 295.1187 still provides sufficient notice. Therefore, the Department deleted draft subdivisions (b)(2) and (c) from emergency Regulation 3802 to avoid any issue regarding the scope of the emergency regulation. However, their deletion does not change the Legal Division’s long-standing opinion and the

Department may propose to incorporate that opinion into a regulation if it becomes necessary to do so in the future.

Regulation 1628 currently implements the exclusion for certain transportation charges in subdivision (c)(7) of RTC section 6012 for sales and use tax purposes. The Department intended for subdivisions (b)(3) and (d) of the draft emergency regulation to incorporate the provisions of Regulation 1628 and clarify that charges a purchaser of cannabis or cannabis products must pay a cannabis retailer for delivery by facilities of the retailer are taxable for sales and use tax and cannabis excise tax purposes, unless the charges satisfy all the requirements of subdivision (b)(2) of Regulation 1628. However, the Department determined that it is not necessary to include that clarification in emergency Regulation 3802 at this time because the interested parties indicated that there is no confusion in the cannabis industry regarding the treatment of transportation charges. Therefore, the Department deleted draft subdivisions (b)(3) and (d) from emergency Regulation 3802 because they are unnecessary at this time. The Department also added new subdivision (c) to emergency Regulation 3802 to clarify that for purposes of the cannabis excise tax, “gross receipts” from the retail sale of cannabis or cannabis products excludes certain transportation charges and that Regulation 1628, Transportation Charges, provides guidelines for the exclusion of transportation charges in RTC section 6012. Accordingly, emergency Regulation 3802 still refers readers to Regulation 1628, but it does not further clarify how Regulation 1628 applies for sales and use tax purposes to avoid any issue regarding the scope of the emergency regulation.

The Department deleted draft subdivisions (b)(4) and (e)(1)(A) regarding packaging from emergency Regulation 3802 and deleted the references to optional packaging from emergency Regulation 3802 because some interested parties said that the BPC’s packaging requirements would make it impossible for a cannabis retailer to legally comply with the optional packaging requirement in the draft emergency regulation. After deleting draft subdivisions (b)(2), (3), (4), (c), and (d), the Department renumbered draft subdivisions (b)(5) and (e) as subdivisions (a)(2) and (b).

The Department revised renumbered subdivision (a)(2) to clarify that for purposes of the cannabis excise tax “gross receipts” include any amount the purchaser is required to pay for tangible personal property, including packaging, the purchaser is required to purchase as a condition of the sale of the cannabis or cannabis products. This is because the Department determined that those amounts are required to be included in gross receipts based upon the terms of the retail sale and the wording of subdivision (a) of RTC section 34011.2. The Department also determined that packaging is the same as other tangible personal property for cannabis excise tax purposes. The Department also added examples to renumbered subdivision (a)(2) to avoid confusion. The examples further clarify that 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. Therefore, subdivision (a) of emergency Regulation 3802 does not go beyond the scope of subdivision (a) of RTC section 34011.2 by generally including charges for tangible personal property, other than cannabis or cannabis products, in the base (i.e., measure) subject to the cannabis excise tax.

In addition, the Department revised renumbered subdivision (b)(1) of emergency Regulation 3802 so that it now 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. “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 from the cannabis retailer without purchasing the tangible personal property. “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. This is because the Department determined that RTC section 34011.2 does not require charges for optional tangible personal property to be included in the gross receipts from retail sales by cannabis retailers.

The Department also added examples to revised and renumbered subdivision (b)(1) to further clarify that when a cannabis retailer sells seven-gram jars of XYZ brand Hawaiian Punch strain cannabis flower separately from lighters or pipes, 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, 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. The examples further clarify that emergency Regulation 3802 does not go beyond the scope of subdivision (a) of RTC section 34011.2 by generally including charges for tangible personal property, other than cannabis or cannabis products, in the base subject to the cannabis excise tax.

Finally, the Department deleted the rebuttable presumption from renumbered subdivision (b)(2). This is because the Department determined that it was unnecessary to add the rebuttable presumption to the provisions regarding the burden of proof in subdivision (b)(2), since the cannabis retailer has the burden of maintaining the records necessary for the Department to determine the taxability of any given transaction.

*Adoption of Emergency Regulation 3802*



The Department adopted revised Regulation 3802, as an emergency regulation, because the Department determined that the adoption of Regulation 3802, as an emergency regulation, is reasonably necessary to have the effect and accomplish the objective of addressing:

- The issue (or problem) regarding how the cannabis excise tax imposed by RTC section 34011.2 applies to charges for other tangible personal property purchased with cannabis or cannabis products in a retail sale;
- The confusion about whether subdivision (i) of Regulation 3700 applies when determining whether charges for cannabis accessories as defined in HSC section 11018.2, including packaging, are included in gross receipts for purposes of the cannabis excise tax imposed by RTC section 34011.2; and
- The 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 anticipates that the adoption of emergency Regulation 3802 will promote fairness and benefit cannabis retailers, purchasers of cannabis or cannabis products, and the Department by clarifying how the cannabis excise tax imposed by RTC section 34011.2 applies to charges for other tangible personal property purchased with cannabis or cannabis products in a retail sale and clarifying 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 has performed an evaluation of whether emergency Regulation 3802 is inconsistent or incompatible with existing state regulations and determined that the emergency regulation is not inconsistent or incompatible with existing state regulations. This is because there are no other regulations that clarify the meaning of "gross receipts of any retail sale by a cannabis retailer" for purposes of the cannabis excise tax imposed by RTC section 34011.2. In addition, the Department has determined that there are no comparable federal regulations or statutes to emergency Regulation 3802.

#### DOCUMENTS RELIED UPON

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

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

The Department has determined that the adoption of emergency Regulation 3802 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 GC.

#### ONE-TIME COST TO THE DEPARTMENT, BUT NO OTHER COST OR SAVINGS TO ANY STATE AGENCY, LOCAL AGENCY, OR SCHOOL DISTRICT

The Department has determined that the adoption of emergency Regulation 3802 will result in an absorbable \$484 one-time cost for the Department to update its website after the emergency rulemaking process is completed (assuming that average hourly compensation costs are \$60.55 per hour and that it will take approximately eight hours). The Department has determined that the adoption of emergency Regulation 3802 will result in no other direct or indirect cost or savings to any state agency, no cost to 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 GC, no other non-discretionary cost or savings imposed on local agencies, and no cost or savings in federal funding to the State of California.

#### EFFECTIVE PERIOD

Subdivision (e) of RTC section 34013 provides that the emergency regulations adopted by the Department to implement, administer, and enforce the CTL may remain in effect for two years from adoption and may be readopted in accordance with subdivision (h) of GC section 11346.1. Therefore, emergency Regulation 3802 shall be effective immediately upon filing with the Secretary of State and shall remain in effect for two years from that date, unless the Department amends or repeals the regulation before the expiration of the two-year period.

#### CONTACT PERSON

Questions about emergency Regulation 3802 should be directed to Ms. Sarah Smith, Business Taxes Specialist II, by telephone at 916-309-5292 or by email at [BTFD-BTC.InformationRequests@cdtfa.ca.gov](mailto:BTFD-BTC.InformationRequests@cdtfa.ca.gov).