

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION

215.0610

LEGAL DIVISION, APPEALS SECTION

In the Matter of the Petition )  
for Redetermination Under the ) DECISION AND RECOMMENDATION  
Sales and Use Tax Law of: )  
)  
B--- of --- --- , Inc. ) No. SR ---B XX-XXXXXXX-010  
)  
)  
Petitioner )

The Appeals conference in the above-referenced matter was held by Senior Staff Counsel James E. Mahler on September 1, 1995, in New York, New York.

Appearing for Petitioner: F--- W---  
State and Local Tax Manager

Appearing for the Sales and Use Tax Department: Steven Fisher  
Supervising Tax Auditor  
Earl C. Chang  
Senior Tax Auditor

Type of Business: automobile distributor

Protested Item

The protested tax liability for the period April 1, 1989, through June 30, 1992, net reaudit adjustments, is measured by:

<u>Item</u>	<u>State, Local and County</u>	<u>Transit</u>	<u>EQRF</u>
B. Demonstration cars loaned to persons over one year	\$520,663	\$687,011	\$213,898

### Petitioner's Contention

The cars loaned to S--- B--- A--- Driving School were frequently demonstrated and displayed while being held for resale in the regular course of business. The measure of tax on such vehicles should therefore be calculated by the 1/40th formula.

### Summary

Petitioner buys new [B] cars from the manufacturer for resale to dealers. During the audit period, it registered a number of these cars in its own name and loaned them to the S--- B--- A--- Driving School (hereinafter "the school") for use in driver training classes in California.

According to newspaper articles, the school offers "specialized instruction in high-performance driving ... that bridges the gap between high-school driver's ed and real-world emergencies...." Students are admitted to the school free, but by invitation only. Most invitations are issued by [B] dealers, who sponsor the classes.

Petitioner wrote a memo to dealers to encourage them to use the school to promote sales of [B]s. Among other thing, the memo points out that a day at the school can induce a customer to buy a [B], give "qualified prospects" the "ultimate test drive", and help close the sale with a prospective buyer. Petitioner also prepared posters, videotapes and print ads touting its relationship with the school and inviting interested persons to visit their local dealer for more information. Petitioner believed that the ad campaign in association with the school would promote the image of [B]s as high-performance vehicles.

Petitioner reported and paid tax on these vehicles measured by the fair rental value for the period of the loan, and used 1/40th of the purchase price to calculate the fair rental value. The audit staff concluded that the tax should have been measured by the full purchase price. Although these vehicles were scheduled in an Audit Item captioned "Demonstration cars loaned to persons over one year", we understand that none of the vehicles was actually on loan for more than 12 months.

### Analysis and Conclusions

Subdivision (b)(3) of Sales and Use Tax Regulation 1669.5 provides in part:

"(A) When a vehicle dealer or lessor assigns a vehicle for a period not exceeding 12 months to employees or officers other than vehicle sales personnel ... the measure of tax is the fair rental value of the vehicle ... [which is] 1/40th of the purchase price of the vehicle for each month of combined demonstration or display and use.

“(B) When a vehicle dealer or lessor assigns a vehicle to persons other than employees or officers, such as relatives or business associates ... [t]ax must be paid measured by the purchase price of such vehicles.”

By its terms, subdivision (b)(3) applies only to vehicle dealers and lessors. Subdivision (c) of the regulation applies to “vehicle manufacturers and distributors” and states in part:

“(2) VEHICLES ASSIGNED FOR LIMITED PERIODS OF TIME. It will be presumed that any vehicle assigned to one or a series of employees or other persons for a period of time not exceeding 12 months in the aggregate is frequently demonstrated or displayed and that it is also used partly for other purposes. This same presumption will be made with respect to any vehicle registered in the name of the manufacturer or distributor, and any vehicle placed for a period of time not exceeding 12 months in a "pool" from which vehicles are assigned to various employees or loaned for short intervals to television studios, visiting dignitaries, automotive magazine editors, etc. Under these circumstances, the measure of tax is the fair rental value of the vehicle for the periods of personal or business use which are interspersed with the demonstration or display. It will be further presumed that the fair rental value for such personal or business use is 1/40th of the ‘net dealer price’ of the vehicle for each month of such combined use.” (Emphasis added.)

Paragraph 0606.27 in Chapter Six of the Board’s Audit Manual provides:

“When cars are loaned to persons who are not customers awaiting delivery of a car purchased or leased from the dealer, or the return of the customer’s car being repaired by the dealer, there is no provision to measure use tax liability by other than the purchase price....”

The audit staff relies on this paragraph of the Audit Manual to argue that petitioner’s tax liability must be measured by the purchase price of the vehicles. However, Chapter Six of the Audit manual is entitled “Motor Vehicle Dealers”, and does not purport to apply to distributors. The cited paragraph is an interpretation of Regulation 1669.5, subdivision (b)(3), which concerns vehicle dealers and lessors, not an interpretation of subdivision (c)(2), which concerns vehicle manufacturers and distributors.

Since petitioner is a distributor, the controlling authority is subdivision (c)(2) of Regulation 1669.5. Under that provision, the tax may be measured by fair rental value when vehicles are loaned to employees or “other persons” for periods not exceeding 12 months for frequent demonstration and display. The term “other persons” means “persons other than employees”, and is further described in the regulation to include “television studios, visiting

dignitaries, automotive magazine editors, etc.” The S--- B--- A--- Driving School is an “other person” for purposes of this subdivision.

The staff also questions whether the vehicles loaned to the school were frequently demonstrated and displayed. However, subdivision (c)(2) of Regulation 1669.5 expressly presumes that vehicles registered in the name of the distributor, as these vehicles were, are frequently demonstrated and displayed. Also, the evidence shows that petitioner’s purpose in loaning vehicles to the school was to promote the sale of [B]s. We find that the vehicles were frequently demonstrated and displayed.

Recommendation

Reaudit. Measure the tax on vehicles registered in petitioner’s name and loaned to the S--- B--- A--- Driving School by the 1/40th formula, if the loan was for a period not exceeding 12 months, or by the purchase price if the loan was for a period of 12 months or more.

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James E. Mahler, Senior Staff Counsel

January 3, 1995  
Date