

TITLE 18. CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION

The California Department of Tax and Fee Administration Proposes to Adopt Amendments to Section 4076, *Wholesale Cost of Tobacco Products*, and New Section 4077, *Tobacco Product Manufacturer*, in Title 18 of the California Code of Regulations

NOTICE IS HEREBY GIVEN that the California Department of Tax and Fee Administration (CDTFA), pursuant to the authority vested in it by Revenue and Taxation Code (RTC) section 30451, proposes to amend California Code of Regulations, title 18, section (Regulation or Reg.) 4076, *Wholesale Cost of Tobacco Products*, and adopt Regulation 4077, *Tobacco Product Manufacturer*. The proposed amendments to Regulation 4076 provide additional notice that the meaning of the term “tobacco products” changed and includes “electronic cigarettes,” for purposes of the taxes and surtaxes imposed under the Cigarette and Tobacco Products Tax Law (CTPTL) (Rev. & Tax. Code (RTC), § 30001 et seq.), effective April 1, 2017. The proposed amendments to Regulation 4076 clarify the meaning of the phrase “sold in combination with,” which is used in the definition of electronic cigarettes, provide examples of items that are and are not electronic cigarettes, clarify how to determine the wholesale cost of tobacco products when the manufacturer is also the distributor, and provide examples of how to estimate or calculate the wholesale cost of products included in the new definition of tobacco products. The proposed amendments to Regulation 4076 clarify that tobacco products may only be distributed once and that a retailer does not make a taxable distribution by repackaging tax-paid tobacco products with other items for retail sale or selling tax-paid tobacco products with other items for a single price at retail. The proposed amendments to Regulation 4076 also replace the regulation’s references to the State Board of Equalization (BOE) with references to the CDTFA. Proposed Regulation 4077 defines the term “tobacco product manufacturer,” clarifies who is regarded as the manufacturer of an electronic cigarette produced by mixing liquid nicotine with flavoring to make a customized product, and clarifies that a retailer who is not a licensed manufacturer or distributor must purchase its nicotine products from a licensed tobacco products distributor or wholesaler.

AUTHORITY

Regulations 4076 and 4077: RTC section 30451

REFERENCE

Regulation 4076: RTC sections 30008, 30010, 30011, 30017, 30105, 30121, 30123, 30126, 30131.1, 30131.2, 30131.5, 30201, and 30221

Regulation 4077: RTC sections 30008, 30010, 30011, 30016, 30103, 30121, 30131.1, 30149, 30210, 30211, and 30212

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

Summary of Existing Laws and Regulations

2017 Legislation

The CTPTL currently imposes taxes and surtaxes on distributors' distributions of cigarettes and other tobacco products (OTP) in this state. The Cigarette and Tobacco Products Licensing Act of 2003 (Licensing Act) (Bus. & Prof. Code (BPC), § 22970 et seq.) currently requires distributors, manufacturers, importers, wholesalers, and retailers of cigarettes and tobacco products to obtain licenses to engage in the sale of cigarettes or tobacco products in this state. (BPC, §§ 22972, 22975, 22979, 22979.21.)

The CTPTL and the Licensing Act were administered and enforced by the BOE pursuant to RTC section 30451 and BPC section 22971.2, respectively. However, on June 27, 2017, the Governor approved Assembly Bill No. (AB) 102 (Stats. 2017, ch. 16), *The Taxpayer Transparency and Fairness Act of 2017*, which added part 8.7 (commencing with section 15570) to division 3 of title 2 of the Government Code (part 8.7). Part 8.7 established the CDTFA (Gov. Code, § 15570) and transferred most of the BOE's former duties, powers and responsibilities to the CDTFA, operative July 1, 2017, including the BOE's former duties, powers, and responsibilities related to the administration and enforcement of the CTPTL and Licensing Act. (Gov. Code, § 15570.22). Part 8.7 provided for the laws prescribing the powers, duties and responsibilities transferred to the CDTFA, including the CTPTL and Licensing Act, and the regulations adopted under those laws to continue in force on and after July 1, 2017. (*Ibid.*) And, part 8.7 provides that "whenever any reference to the [BOE] appears in any statute, regulation, or contract, or in any other code, with respect to any of the functions transferred to the [CDTFA], it shall be deemed to refer to the [CDTFA]." (Gov. Code, § 15570.24).

Distributors, Manufacturers, Importers, Wholesalers, and Retailers

As relevant here, the CTPTL currently provides that the term "distribution" includes "[t]he sale of untaxed cigarettes or tobacco products in this state" and "[t]he placing . . . of untaxed cigarettes or tobacco products . . . in retail stock for the purpose of selling the cigarettes or tobacco products to consumers." (RTC, § 30008, subds. (a) & (c).) The CTPTL currently provides that the term "distributor" includes every person who distributes cigarettes or tobacco products, "within the meaning of the term 'distribution.'" (RTC, § 30011, subds. (a) & (b).) And, it generally provides that "untaxed" cigarettes and tobacco products means cigarettes and tobacco products that have not been distributed in such a manner as to produce a tax liability under the CTPTL. (RTC, §§ 30005, 30005.5.)

The CTPTL currently requires distributors to register for a distributor's license (RTC, §§ 30140, 30151) and makes it a crime to engage in business as a distributor without a license. (RTC, § 30149.) The CTPTL requires distributors to purchase tax stamps to pay the taxes imposed on their distributions of cigarettes, and affix a tax stamp to each pack of cigarettes before distribution. (RTC, §§ 30161, 30163.) It also requires distributors to file returns reporting the taxes imposed on their distributions of OTP, and requires distributors to remit payment for those taxes with their returns. (RTC, § 30181, subd. (b).) And, tobacco products are referred to as "tax-paid" after they have been distributed by a licensed distributor who will pay the applicable taxes imposed on the distribution of the tobacco products under the CTPTL.

The CTPTL does not prohibit manufacturers from buying untaxed materials to use to manufacture cigarettes and tobacco products, and provides for manufacturers to sell untaxed cigarettes and tobacco products to licensed distributors (RTC, § 30103), although there are no CTPTL statutes or regulations that define the term “manufacturer” or clarify which persons are considered to be tobacco product manufacturers. The CTPTL provides for the original importer (as defined in RTC, § 30019) to sell untaxed cigarettes and tobacco products manufactured outside the United States to a licensed distributor. (RTC, § 30105.) The CTPTL provides that the term “wholesaler” includes any person, other than a licensed distributor, who engages in the business of making sales for resale of tax-paid cigarettes and tobacco products (RTC, § 30016), requires wholesalers to register for a wholesaler’s license (RTC, § 30155), and makes it a crime to engage in business as a wholesaler without a license. (RTC, § 30159.) The CTPTL also provides that if any person becomes a distributor without first obtaining a distributor’s license, then the taxes and applicable penalties and interest, imposed on the person’s distributions of untaxed cigarettes and OTP are immediately due and payable (RTC, § 30210), and the taxes, interest, and penalties are subject to being immediately assessed and collected by the seizure and sale of the person’s property. (RTC, §§ 30211, 30212.) The CTPTL does not define the term “retailer” and the CTPTL does not apply to a retailer, unless the retailer is also a distributor, manufacturer, importer, or wholesaler.

Taxes and Surtaxes on Distributors’ Distributions of Cigarettes and Tobacco Products

RTC section 30101 in the CTPTL imposes a tax upon every distributor of cigarettes and the tax applies to the distribution of each cigarette. The rate of the RTC section 30101 tax was five mills (\$0.005) per cigarette distributed from October 1, 1967, through December 31, 1993, and the rate of the tax has been six mills (\$0.006) per cigarette or \$0.12 per pack (\$0.006 x 20 cigarettes) distributed since January 1, 1994.

In November 1988, California voters passed Proposition 99, known as the “Tobacco and Health Protection Act of 1988” (Prop. 99). Among other things, Prop. 99 imposed a surtax on every distributor of cigarettes at the rate of 12.5 mills (\$0.0125) per cigarette or \$0.25 per pack (\$0.0125 x 20 cigarettes) distributed. Prop. 99 imposed a tax on every distributor of OTP, based on the wholesale cost of the products distributed, at a rate equivalent to the combined rate of the taxes imposed on cigarettes by the Prop. 99 surtax and the other provisions of the CTPTL, which only included the RTC section 30101 tax at the time. Prop. 99 also added RTC section 30121, subdivision (b), to the CTPTL to provide that OTP “includes, but is not limited to, all forms of cigars, smoking tobacco, chewing tobacco, snuff, and any other articles or products made of, or containing at least 50 percent, tobacco, but does not include cigarettes.” Prop. 99’s surtax on the distribution of cigarettes and equivalent tax on the distribution of OTP are both codified in RTC section 30123 in the CTPTL.

In November 1998, California voters passed Proposition 10, known as “The Children and Families First Act” (Prop. 10). The purpose of Prop. 10 was to create county commissions to provide early childhood medical care and education. Prop. 10 imposed an additional surtax on every distributor of cigarettes at the rate of 25 mills (\$0.025) per cigarette or \$0.50 per pack distributed. Prop. 10 imposed a tax on every distributor of OTP (as defined in RTC, § 30131.1, subd. (b), which was identical to RTC, § 30121, subd. (b) quoted above), based on the wholesale cost of the products distributed, at a rate equivalent to the rate of the Prop. 10 surtax on

cigarettes. Prop. 10's surtax on the distribution of cigarettes and equivalent tax on the distribution of OTP are both codified in RTC section 30131.2 in the CTPTL.

On November 8, 2016, California voters passed Proposition 56, known as "The California Healthcare, Research and Prevention Tobacco Tax Act of 2016" (Prop. 56), which went into effect on April 1, 2017. As relevant here, Prop. 56 imposed an additional tax on every distributor of cigarettes at the rate of 100 mills (\$0.10) per cigarette or \$2.00 per pack distributed, which increased the combined cigarette tax rate from \$0.87 per pack to \$2.87 per pack. And, Prop. 56 imposed a tax on every distributor of OTP based on the wholesale cost of the products, at a rate equivalent to the rate of Prop. 56's tax on cigarettes. Prop. 56's tax on the distribution of cigarettes is codified in RTC section 30130.51 in the CTPTL and Prop. 56's equivalent tax on the distribution of OTP is imposed by RTC section 30123 in the CTPTL (discussed above).

In addition, Prop. 56 amended RTC section 30121, subdivision (b), to provide, for purposes of Prop. 99's tax on OTP, that:

"Tobacco products" includes, but is not limited to, a product containing, made, or derived from tobacco or nicotine that is intended for human consumption, whether smoked, heated, chewed, absorbed, dissolved, inhaled, snorted, sniffed, or ingested by any other means, including, but not limited to, cigars, little cigars, chewing tobacco, pipe tobacco, or snuff, but does not include cigarettes. Tobacco products shall also include electronic cigarettes. Tobacco products shall not include any product approved by the United States Food and Drug Administration for sale as a tobacco cessation product or for other therapeutic purposes where that product is marketed and sold solely for such approved use. Tobacco products does not include any food products as that term is defined pursuant to Section 6359.

Prop. 56 added a new subdivision (c) to RTC section 30121 to provide, for purposes of Prop. 99's tax on OTP, that:

"Electronic cigarettes" means any device or delivery system sold in combination with nicotine which can be used to deliver to a person nicotine in aerosolized or vaporized form, including, but not limited to, an e-cigarette, e-cigar, e-pipe, vape pen, or e-hookah. Electronic cigarettes include any component, part, or accessory of such a device that is used during the operation of the device when sold in combination with any liquid or substance containing nicotine. Electronic cigarettes also include any liquid or substance containing nicotine, whether sold separately or in combination with any device that could be used to deliver to a person nicotine in aerosolized or vaporized form. Electronic cigarettes do not include any device not sold in combination with any liquid or substance containing nicotine, or any battery, battery charger, carrying case, or other accessory not used in the operation of the device if sold separately.

And, Prop. 56 amended RTC section 30131.1 and added RTC section 30130.50, so that OTP has the same meaning for purposes of Prop. 10's and Prop. 56's taxes on OTP, as it does for Prop. 99's tax on OTP, after the amendments to RTC section 30121 quoted above.

Wholesale Cost

RTC section 30017 provides that “[w]holesale cost’ means the cost of tobacco products to the distributor prior to any discounts or trade allowances.” On May 24, 2016, the BOE adopted Regulation 4076 to clarify the meaning of the phrase “wholesale cost,” and the regulation became effective October 1, 2016.

As relevant here, Regulation 4076, subdivision (a)(3), currently provides that “[f]inished tobacco products’ and tobacco products in ‘finished condition’ are tobacco products that will not be subject to any additional processing before first distribution in the state.” Regulation 4076, subdivision (b)(2), currently explains how to determine the wholesale cost of OTP when a manufacturer or importer is also the distributor. It provides that the wholesale cost of OTP “includes all manufacturing costs, the cost of raw materials (including waste materials not incorporated into the finished tobacco product) prior to any discounts or trade allowances, the cost of labor, any direct and indirect overhead costs, any direct (including freight-in) and indirect overhead costs, and any federal excise and/or U.S. Customs taxes paid. Wholesale cost includes all freight or transportation charges for shipment of materials and/or unfinished product from the supplier to the manufacturer concurrently licensed as a distributor, but excludes domestic freight or transportation charges for shipment of finished tobacco products.” Regulation 4076, subdivision (b)(3) and (4), currently provide that “[i]f tobacco product costs include express, implicit, or unstated discounts or trade allowances” or “[i]f tobacco products are not purchased in an arm’s-length transaction,” “the correct wholesale costs to be reported by the distributor may be determined using any of the methods in subdivision (c).” Regulation 4076, subdivision (c), currently provides alternative methods for determining the wholesale cost of OTP using available price lists or industry data, and Regulation 4076, subdivision (c)(2)(E), currently provides for the use of additional methods with BOE approval. Regulation 4076, subdivision (d), currently presumes that transactions between related parties are not at arm’s-length and explains how to rebut the presumption if the BOE determines that a transaction is between related parties. Regulation 4076, subdivision (e), currently provides seven examples about how to calculate the wholesale cost of OTP under different circumstances, the example in subdivision (e)(1) concerns a distributor who produces handmade cigars, and the example in subdivision (e)(2) concerns a transaction between related parties that the BOE presumes is not at arm’s-length. And, Regulation 4076, subdivision (f), currently explains that the BOE’s “annual determination of the rate of tax that applies to other tobacco products shall be made based on the wholesale cost of tobacco products as of March 1 of the current calendar year and shall be effective during the next fiscal year, beginning July 1,” in accordance with the express provisions of RTC sections 30126 and 30131.5 in the CTPTL.

Initial Need for Regulatory Action

The passage of Prop. 56 changed the definition of OTP and included electronic cigarettes in the definition of OTP for the first time. Therefore, BOE staff determined that distributors may have issues (or problems within the meaning of Gov. Code, § 11346.2, subd. (b)(1)) understanding that the definition of OTP changed, effective April 1, 2017, determining whether certain items are electronic cigarettes subject to the taxes on OTP, and determining the wholesale cost of electronic cigarettes subject to the taxes on OTP. And, BOE staff determined that it is necessary to amend Regulation 4076 for the specific purpose of addressing the issues (or problems) by providing additional notice to distributors regarding the new definition of OTP, clarifying the new definition of OTP by defining the phrase “sold in combination with,” which is used in the definition of electronic cigarettes, and providing examples of how to estimate or calculate the wholesale cost of products that have been defined as OTP effective April 1, 2017.

Prop. 56 did not change the CTPTL’s definition of cigarettes and BOE staff was not aware of any confusion regarding Prop 56’s additional tax on the distribution of cigarettes. So, BOE staff determined that there was no need to take regulatory action to further clarify the application of the cigarette taxes imposed by the CTPTL due to the passage of Prop. 56.

Initial Definition of Sold in Combination With

As noted above, RTC section 30121, subdivision (c), provides that “[e]lectronic cigarettes” means any device or delivery system sold in combination with nicotine which can be used to deliver to a person nicotine in aerosolized or vaporized form” and includes “any component, part, or accessory of such a device that is used during the operation of the device when sold in combination with any liquid or substance containing nicotine.” BOE staff visited manufacturers’ websites prior to April 1, 2017. BOE staff noted that manufacturers commonly sold vaping devices with related products, including liquids and substances containing nicotine, directly to consumers as part of starter kits or all-in-one kits for a single price. BOE staff noted that manufacturers allowed customers to choose whether to include nicotine in their start kits or all-in-one kits and to choose the percentage of nicotine included in kits with nicotine. BOE staff also noted that some manufacturers sell the same items included in starter kits and all-in-one kits individually, such as vaping devices, components, accessories, and liquids or substances containing nicotine, and they will sell the individual items for separately stated prices in the same transaction. Therefore, BOE staff determined that the phrase sold in combination with does not refer to “every” item that is merely sold “with” a liquid or substance containing nicotine in the same transaction based upon the wording of RTC section 30121, subdivision (c), and industry practice. Staff determined that when a kit containing a device or delivery system that can be used to deliver nicotine in aerosol or vapor form to a person or a kit containing any component, part, or accessory of such a device or delivery system is sold with any liquid or substance containing nicotine for a single price, then the items are sold in combination with the liquid or substance containing nicotine and the entire unit is an electronic cigarette for purposes of section 30121, subdivision (c). Staff determined that when a kit containing a device or delivery system or a kit containing any component, part, or accessory of such a device or delivery system is not sold with a liquid or substance containing nicotine for a single price, the kit is not an electronic

cigarette. Staff also determined that when the individual items that can be included in a kit are sold in the same transaction for separately stated prices, then the items are not sold in combination with each other for purposes of RTC section 30121, subdivision (c), and only the liquids or substances containing nicotine would be electronic cigarettes. The other items would not be electronic cigarettes.

First Discussion Paper and Interested Parties Meeting

As a result, BOE staff drafted amendments to Regulation 4076 to address the issues described above, staff prepared a discussion paper explaining the proposed amendments, and staff issued the discussion paper on March 27, 2017. The proposed amendments:

- Added new subdivision (a)(3) to define the term “electronic cigarettes” in accordance with RTC section 30121, subdivision (c);
- Renumbered current subdivision (a)(3) as subdivision (a)(4);
- Added new subdivision (a)(5) to clarify that the term “sold in combination with” refers to kits, systems, or packages that usually include atomizers, cartomizers or similar type device, component pieces, accessories, and liquids containing nicotine that are all sold for a single price”;
- Added new subdivision (a)(6) to explain that the definition of OTP changed effective April 1, 2017, and now “includes all products containing, made, or derived from tobacco or nicotine that are intended for human consumption,” including electronic cigarettes, but does not include cigarettes; and
- Added new subdivision (f) to provide examples of how to estimate or calculate the wholesale cost of products that have been defined as OTP effective April 1, 2017, such as self-manufactured nicotine products, kits sold with nicotine for a single price, and closed-system electronic cigarettes containing nicotine.

BOE staff held an interested parties meeting to discuss the proposed amendments on April 11, 2017. During the meeting, BOE staff indicated that they were proposing to change the “definition of sold in combination with” to refer to “kits, systems, or packages that usually include atomizers, cartomizers or similar type device, component pieces, accessories, and liquids containing nicotine that are *packaged or wrapped as one set or sold for a single price.*” (Italics added.) Staff explained that the change was intended to prevent distributors from selling kits containing devices or delivery systems and liquids containing nicotine as one unit, but separately stating the prices of the items in the kits so that the liquids containing nicotine are the only items in the kits classified as electronic cigarettes and only the wholesale cost of the liquids containing nicotine is subject to tax.

During the April 2017 meeting, BOE staff was asked to clarify who is regarded as the manufacturer of a tobacco product, particularly an electronic cigarette produced by mixing liquid nicotine with flavoring to make a customized product. Also, staff was asked if either Distributor A or B can obtain a refund when Distributor B purchases OTP in California from Distributor A, Distributor A reports and pays its tax on its distribution of the OTP in California, and then

Distributor B subsequently sells the tax-paid OTP to a third party and ships the OTP out of state pursuant to that contract of sale. And, BOE staff said that, under those facts, tax would apply to Distributor A's distribution of the OTP in California and Distributor B could not obtain a refund of tax reported and paid by Distributor A, even if it was refundable to Distributor A.

After the April 2017 meeting, Nu Mark LLC submitted a written comment dated April 25, 2017, suggesting that BOE staff's proposed definition of electronic cigarettes was too broad and that a component, part, or accessory of a device or delivery system should only be classified as an electronic cigarette if it is sold in combination with nicotine and it is used during the operation of the device or delivery system, based upon the second sentence in RTC section 30121, subdivision (c) (quoted above). However, BOE staff disagreed and concluded that a component, part, or accessory of a device or delivery system that is not used in the operation of the device or delivery system is still an electronic cigarette if it is sold in combination with a liquid or substance containing nicotine because the fourth sentence in RTC section 30121, subdivision (c), expressly provides that "[e]lectronic cigarettes do not include . . . any battery, battery charger, carrying case, or other accessory not used in the operation of the device *if sold separately.*" (Italics added.)

In its written comment, Nu Mark LLC also agreed that items should be considered to be sold in combination with each other if they are packaged together as one set or unit. However, Nu Mark LLC did not agree that items should be considered to be sold in combination with each other solely because they are sold for a single price. And, Nu Mark LLC expressed its concern that staff's proposed definition of sold in combination was too broad and recommended that the phrase "or sold for a single price" be deleted from the definition so that tax would only apply to the wholesale cost of the liquid containing nicotine when a distributor offers to sell a separately packaged device and a separately packaged liquid containing nicotine for a single price or offers a free device to customers who purchase a specified amount of liquid containing nicotine, as a promotion.

In addition, the California Smoke Free Organization (CSFO) submitted a written comment dated April 26, 2017, agreeing that the definition of sold in combination with should include items sold with a liquid containing nicotine "as one set in [their] original manufactur[er] packaging, or packaged or wrapped as one set or sold for a single price by a licensed distributor," and suggesting that the definition should not include items a retailer purchases separately and for a separate price, no matter how the items are sold by the retailer. CSFO said that its suggested language was intended to "protect retailers [that are not licensed distributors] from being considered de facto distributors if they package or wrap nicotine substances and devices as one set or sell them for a single price at the retail level." Also, CSFO's written comment concluded that, in its opinion, "if Distributor A applies tax to its distribution of tobacco products to Distributor B, then Distributor B ships the tax paid tobacco products pursuant to a contract of sale [with a third party] to a point outside this state, either Distributor B or at least Distributor A, should be able to obtain a refund or credit" under RTC section 30176.1 and Regulation 4063.5, *Exported Tax-Paid Tobacco Products*, or RTC section 30361.5, and suggested that Regulation 4063.5 should be clarified accordingly. And, Californians for Tobacco Harm Reduction (CATHR) submitted a written comment dated April 24, 2017, asking BOE staff to clarify how the proposed definition of sold in combination with applies at the retail level.

Second Issue Paper and Second Interested Parties Meeting

After considering the interested parties comments, BOE staff determined that manufacturers commonly sell vaping devices with related products, including liquids and substances containing nicotine, as part of starter kits or all-in-one kits. Some manufacturers also allow customers to create customized kits by selecting their accessories, flavoring, and nicotine content. And, the manufacturers package the products included in a kit all together in a single box or other type of storage container, which is sealed by the manufacturer, and which lists the contents of the kit and includes the manufacturer's logos, pictures, and advertisements on the outside of the box or container. Therefore, BOE staff agreed with CSFO that an item is sold in combination with a liquid or substance containing nicotine when they are sold together in their original manufacturer packaging as one unit. And, to address Nu Mark LLC's and CSFO's concerns, BOE staff agreed to change the definition of sold in combination with to refer to "kits, systems, or packages that usually include atomizers, cartomizers or similar type device, component pieces, accessories, and liquids containing nicotine that are *sold in their original manufacturer packaging as one unit* or sold for a single price" (italics added), so that items a retailer purchases separately for a separate price and packages with tax-paid liquid containing nicotine would not be considered sold in combination with the nicotine merely because they were packaged together by the retailer, and retailers that are not licensed distributors would not be considered de facto distributors just because they packaged an item together with a tax-paid liquid containing nicotine as one unit for sale at the retail level.

Also, to address Nu Mark LLC's and CSFO's concerns and CATHR's request for further clarification, BOE staff agreed to revise the examples in Regulation 4076, subdivision (f)(2) and (3), to make them consistent with the revised definition of sold in combination with. BOE staff agreed to add new subdivision (f)(5) to Regulation 4076 to provide an example clarifying that when a retailer purchases tax-paid liquid containing nicotine from a licensed distributor and then packages the liquid with other items for sale as part of a promotion, the promotional package is not subject to tax because "the distribution occurred prior to the retail sale." And, BOE staff agreed to add new subdivision (f)(6) to Regulation 4076 to provide an example clarifying that a separately packaged device and a separately packaged liquid containing nicotine are not sold for a single price when the distributor's invoice shows the price charged for each item, even if the price charged for one of the items is zero. However, BOE staff continued to assert that items a distributor sells with a previously un-taxed liquid containing nicotine for a single price are sold in combination with the nicotine under RTC section 30121, subdivision (c), regardless of how they are packaged by the manufacturer or distributor.

In addition, after considering the interested parties comments, BOE staff determined that there may be additional issues (or problems within the meaning of Gov. Code, § 11346.2, subd. (b)(1)) determining whether a person is a manufacturer of OTP, as newly defined, effective April 1, 2017. And, BOE staff determined that it was necessary to propose a new regulation for the specific purpose of addressing the additional issues by defining the term "tobacco product manufacturer" and clarifying who is regarded as the manufacturer of an electronic cigarette produced by mixing liquid nicotine with flavoring to make a customized product. Therefore, BOE staff looked at federal law for guidance as to who is a manufacturer of tobacco products.

Specifically, BOE staff looked at section 387(20)(A) of title 21 of the United States Code, which provides that “tobacco product manufacturer means any person, including any repacker or relabeler, who . . . manufactures, fabricates, assembles, processes, or labels a tobacco product” for purposes of the Federal Food, Drug, and Cosmetic Act (21 U.S.C. § 301 et seq.). BOE staff drafted subdivision (a) of proposed Regulation 4077, *Tobacco Product Manufacturer*, to define tobacco product manufacturer in accordance with the federal definition and clarify that a “tobacco product manufacturer is any person, including any repacker or relabeler, who manufactures, fabricates, assembles, processes, or labels a finished tobacco product.” BOE staff drafted subdivision (b) of proposed Regulation 4077 to specifically clarify for retailers that a “retailer who mixes, prepares, or combines liquid nicotine and other components of a tobacco product is a tobacco product manufacturer” and “if the retailer does not mix, prepare or combine any liquid nicotine products but allows its customers to do so after a sale has been made then that retailer is not a manufacturer,” based upon the general definition of tobacco product manufacturer. BOE staff also included a third sentence in subdivision (b) of proposed Regulation 4077 to provide additional notice that “A retailer must purchase their nicotine products from a licensed tobacco products distributor” so the retailer will not become a distributor without first obtaining a distributor’s license.

In addition, after considering CSFO’s written comment:

- BOE staff concluded that RTC section 30176.1 only provides for a refund when tax has been “paid on the *distribution* of tobacco products which are shipped to a point outside the state” (italics added) and does not apply when a distributor makes a distribution of OTP in the state and does not ship the products outside the state as part of the distribution in accordance with Regulation 4063.5;
- BOE staff also concluded that RTC section 30361 only permits an amount to be refunded to the distributor who paid it and only if the amount paid was computed upon an amount that is not taxable or the amount paid was in excess of the tax due, and it does not provide for a refund of tax that was properly paid on the distribution of OTP in the state; and
- A statutory change would be required to provide a refund if Distributor A applies tax to its distribution of tobacco products to Distributor B in this state, then Distributor B ships the tax paid tobacco products to a point outside this state pursuant to a contract of sale with a third party.

As a result, BOE staff prepared a second discussion paper explaining its revised amendments to Regulation 4076, staff’s new proposed Regulation 4077, and staff’s understanding of RTC sections 30176.1 and 30361. Staff issued the second discussion paper, the revised amendments to Regulation 4076, and proposed Regulation 4077 on May 26, 2017. And, staff held an interested parties meeting to discuss the revised amendments and proposed regulation on June 6, 2017.

At the June 2017 interested parties meeting, BOE staff was informed by the electronic cigarette industry that when the owner of a brand or formula for a type of liquid nicotine manufactures its product, the owner of the brand or formula may contract with another person to complete the fabrication and assembly of the product to the brand or formula owner’s standard. Staff was also informed that the industry refers to the owner of a brand or formula for a type of liquid nicotine

as a manufacturer regardless of whether the owner directly performs all of the services related to the manufacture of its product or contracts with a third party to perform services related to the manufacture of its product on its behalf. And, some interested parties raised another issue (or problem within the meaning of Gov. Code, § § 11346.2, subd. (b)(1)) about whether staff's proposed definition of tobacco product manufacturer in Regulation 4077, subdivision (a), was broad enough to classify the owner of a brand or formula for a type of liquid nicotine as a manufacturer when the owner contracts with a third party to perform services related to the manufacture of its product.

After the June 2017 meeting, BOE staff received written comments from SAVEURvape, Inc., and Ting Fan, which were both dated June 20, 2017, and recommended that the definition of tobacco product manufacturer in Regulation 4077, subdivision (a), be revised to include the owner of a "brand and formula" for a tobacco product who contracts with a third party to perform services related to the manufacture of its product. BOE staff also received written comments from Charlie's Chalk Dust, LLC, and CSFO, which were both dated June 22, 2017, and recommended that the definition of tobacco product manufacturer include a tobacco "product owner" and "product licensee" who contracts with a third party to perform services related to the manufacture of its product.

In addition, CSFO's June 2017 written comment recommended that Regulation 4076 do more to clarify that a retailer who packages untaxed devices or other items with tax-paid liquid containing nicotine and sells them for a single price will not be considered a distributor.

The comment requested that staff further clarify how a person that is both the manufacturer and distributor of electronic cigarettes is required to calculate the wholesale cost of the electronic cigarettes under Regulation 4076, subdivision (b)(2). The comment recommended that the third sentence in proposed Regulation 4077, subdivision (b), be revised to clarify that a retailer "that is not also a manufacturer or distributor" must purchase their nicotine products from a licensed tobacco products distributor. And, the comment disagreed with BOE staff's analysis of RTC sections 30176.1 and 30361 and Regulation 4063.5, and requested that Regulation 4063.5 be amended to clarify that a refund is permitted if Distributor A applies tax to its distribution of tobacco products to Distributor B in the state, then Distributor B ships the tax paid tobacco products for subsequent sale or use outside this state.

CDTFA Staff's Changes to the Proposed Amendments to Regulation 4076

CDTFA staff continued to work on BOE staff's project to amend Regulation 4076 and adopt new Regulation 4077 after the July 1, 2017, transfer of the BOE's authority to administer and enforce the CTPTL to the CDTFA. CDTFA staff determined that there was another issue (or problem within the meaning of Gov. Code, § § 11346.2, subd. (b)(1)) with Regulation 4076 because it refers to the BOE, instead of the CDTFA, as the agency with the authority to administer and enforce the CTPTL. Therefore, CDTFA staff proposed replacing the references to the BOE with references to the CDTFA in Regulation 4076, subdivisions (c)(2)(E), (d)(2), and (e)(2), and renumbered subdivision (g), to address the issue.

In addition, CDTFA staff considered the interested parties' comments from June 2017. And, CDTFA staff determined that Regulation 4076, subdivision (b)(2), should more clearly explain

what overhead costs are includable in a manufacturer's manufacturing costs and generally permit manufacturers and importers to use the alternative methods in Regulation 4076, subdivision (c), to determine the wholesale cost of OTP. Therefore, CDTFA staff proposed deleting the phrase providing that manufacturing costs include "any direct (including freight-in) and indirect overhead costs" from the first paragraph in subdivision (b)(2) and adding a new second paragraph to subdivision (b)(2) to more clearly explain that:

Manufacturing costs include all overhead expenses that are directly or indirectly attributable to the production of finished goods. These costs can include, but are not limited to, production and administrative salaries, depreciation, repairs and maintenance, rent and utilities for the production facilities, and equipment. Manufacturing costs must be allocated to each product unit by a reasonable and consistent pro-rata accounting method. Manufacturing costs do not include overhead expenses that are not directly or indirectly attributable to the production of finished goods. These costs can include, but are not limited to, salaries and other expenses for business activities involving selling, distribution, marketing, finance, information technology, human resources and legal activities.

CDTFA staff proposed adding a new fourth paragraph to Regulation 4076, subdivision (b)(2), to permit manufacturers and importers that are also distributors to use the alternative methods in Regulation 4076, subdivision (c), to determine the wholesale cost of OTP. CDTFA staff proposed amending the example currently in Regulation 4076, subdivision (e)(1), and the example proposed to be added to Regulation 4076, subdivision (f)(1), to clarify that the distributors in the examples are also manufacturers and the wholesale cost of the OTP they manufacture would include the costs described in subdivision (b)(2). CDTFA staff proposed adding new subdivision (f)(7) to Regulation 4076 to provide an example illustrating that a manufacturer who uses five percent of a rented facility for manufacturing is required to include five percent of the rent paid for the facility in its manufacturing costs. And, CDTFA staff proposed other minor grammatical changes to Regulation 4076, subdivisions (b)(2) and (f)(5) and (6), and renumbered subdivision (g).

CDTFA staff provided a revised draft of the proposed amendments to Regulation 4076 to the interested parties on August 1, 2017. CDTFA staff received a written comment from CATHR dated August 10, 2017. CATHR's comment indicated that some members of the association had received inconsistent information from CDTFA staff about how to substantiate the wholesale cost of OTP when the manufacturer is also the distributor. And, CATHR's comment requested that Regulation 4076 "spell out that there is no requirement that a certain transaction be performed to document the movement of tobacco products from a licensed manufacturer that is also a licensed distributor when they are the same entity" and requested additional "explicit clarification that an arm's length transaction would not be required in this circumstance." CDTFA staff agreed that this new issue was important, and should be addressed through appropriate training and outreach after the current rulemaking project is completed. However, CDTFA staff did not agree that further amendments to Regulation 4076 are needed to address the issue at this time.

CDTFA staff received a written comment from Dr. Michael Ong, dated August 11, 2017, on behalf of the Tobacco Education and Research Oversight Committee, which raised concerns about

whether the proposed regulatory definitions for the terms “electronic cigarettes” and “tobacco products” were too abbreviated and suggested alternative definitions. Therefore, CDTFA staff reviewed the proposed definitions. Staff revised the regulatory definition of electronic cigarettes to clarify that electronic cigarettes include any liquids (“e-juice” or “e-liquid”) or substances that contain nicotine, “regardless of whether they are sold in combination with any device, delivery system, or any component, part, or accessory of such a device or delivery system,” to ensure consistency between the statutory and regulatory definitions and avoid any potential confusion. However, CDTFA staff did not revise the definition of tobacco products because staff determined that the regulatory definition is clear, concise, and consistent with the statutory definition in RTC section 30121 as amended by Prop. 56.

Also, CDTFA staff received a written comment from CSFO dated August 18, 2017. CSFO’s comment requested that the example being added to subdivision (f)(5) of Regulation 4076 be revised to “clarify that tax would not apply to the transaction even if the retailer sold the promotional package for a single price.” CDTFA staff agreed that tax would not apply to the transaction in the example even if the retailer sold the promotional package for a single price and that the example should be clarified accordingly. Staff also realized that the example was illustrating that OTP, such as a liquid or substance containing nicotine, may only be distributed once, and that an item is only sold in combination with a liquid or substance containing nicotine if they are sold in their original manufacturer packaging as one unit or sold for a single price before or when the liquid or substance containing nicotine is distributed. Therefore, staff proposed to delete the word “first” from the definition of “finished tobacco product” and tobacco product in “finished condition” in renumbered subdivision (a)(4) of Regulation 4076 to clarify that there is only one distribution of OTP. Staff revised the definition of sold in combination with proposed to be added to subdivision (a)(5) of Regulation 4076 to provide that an item is sold in combination with a liquid or substance containing nicotine if they are sold in their original manufacturer packaging as one unit or sold for a single price “before or when the liquid or substance containing nicotine is distributed.” Staff also revised the example being added to subdivision (f)(5) of Regulation 4076 to clarify that tax does not apply when a retailer purchases a tax-paid liquid containing nicotine and packages it together with other items for retail sale at a single price as a promotion because the distribution of the tax-paid liquid containing nicotine already occurred.

In addition, CSFO’s August 18, 2017, written comment incorporated its prior comments regarding refunds and requested that Regulation 4063.5 be further clarified. However, CDTFA staff determined that any changes to Regulation 4063.5 would be beyond the scope of the current project to address issues (or problems) related to the passage of Prop. 56 and CDTFA staff did not agree that it is necessary to make any changes to Regulation 4063.5 at this time.

CDTFA Staff’s Changes to Proposed Regulation 4077

After considering the interested parties’ comments from June 2017, CDTFA staff agreed that the owner of a brand or formula for a tobacco product who contracts with another person to physically complete the fabrication and assembly of the product to the brand or formula owner’s standard is a manufacturer. Therefore, CDTFA staff proposed adding the following additional sentence to Regulation 4077, subdivision (a), to address the issue regarding brand or formula owners raised at the June 2017 interested parties meeting:

The term tobacco product manufacturer includes an owner of a brand or formula for a tobacco product who contracts with another person to complete the fabrication and assembly of the product to the brand or formula owner's standard.

In addition, after reviewing CSFO's June 2017 written comment regarding the third sentence in proposed Regulation 4077, subdivision (b), CDTFA staff determined that the statement in the third sentence that a "retailer must purchase their nicotine products from a licensed tobacco products distributor" was not entirely accurate. This is because a retailer that is a licensed manufacturer or distributor may purchase untaxed nicotine products from a person that is not a licensed tobacco products distributor, and making such a purchase will not cause a retailer that is already a licensed manufacturer or distributor to become a distributor without first obtaining a distributor's license. This is also because a retailer that is not a licensed manufacturer or distributor may purchase tax-paid cigarettes and tobacco products from a licensed distributor or wholesaler and doing so will not cause a retailer to become a distributor without first obtaining a distributor's license. Therefore, to be entirely accurate, staff revised the sentence to provide that a "retailer who is not a licensed manufacturer or distributor must purchase its nicotine products from a licensed tobacco products distributor or wholesaler."

Determinations

The CDTFA subsequently determined that staff's proposed amendments to Regulation 4076 are reasonably necessary to have the effect and accomplish the objective of addressing the issues (or problems) regarding the change to the definition of OTP, effective April 1, 2017, determining whether certain items are electronic cigarettes subject to the taxes on OTP, and determining the wholesale cost of electronic cigarettes subject to the taxes on OTP, discussed above, by providing additional notice to distributors regarding the new definition of OTP, clarifying the new definition of OTP by defining the phrase "sold in combination with," which is used in the definition of electronic cigarettes, providing examples of items that are and are not sold in combination with a liquid or substance containing nicotine, clarifying how to determine the wholesale cost of OTP when the manufacturer is also the distributor, and providing examples of how to estimate or calculate the wholesale cost of products that have been defined as OTP effective April 1, 2017. The CDTFA determined that the amendments to Regulation 4076 are reasonably necessary to have the effect and accomplish the objective of addressing the issue (or problem) regarding the references to the BOE in Regulation 4076 by replacing those references with references to the CDTFA. The CDTFA determined that staff's proposed Regulation 4077 is reasonably necessary to have the effect and accomplish the objective of addressing the issue (or problem) determining whether a person is a manufacturer of OTP, as newly defined, effective April 1, 2017, by defining the term "tobacco product manufacturer," and clarifying who is regarded as the manufacturer of an electronic cigarette produced by mixing liquid nicotine with flavoring to make a customized product. The CDTFA also determined that staff's proposed amendments to Regulation 4076 and staff's proposed Regulation 4077 are reasonably necessary to have the effect and accomplish the objective of addressing the de facto distributor issue (or problem) discussed above by clarifying in Regulation 4076 that OTP may only be distributed once and that a retailer does not make a taxable distribution by repackaging tax-paid OTP with other items for retail sale or selling tax-paid OTP with other items for a single price at retail, and clarifying in proposed Regulation 4077 that a retailer who is not a licensed manufacturer or are

reasonably necessary to have the effect and accomplish the objective of distributor must purchase its nicotine products from a licensed tobacco products distributor or wholesaler.

The CDTFA anticipates that the proposed amendments to Regulation 4076 will promote fairness and benefit taxpayers and the CDTFA by providing additional notice to distributors regarding the new definition of OTP, clarifying the new definition of OTP by defining the phrase “sold in combination with,” which is used in the definition of electronic cigarettes, providing examples of items that are and are not sold in combination with a liquid or substance containing nicotine, clarifying how to determine the wholesale cost of OTP when the manufacturer is also the distributor, and providing examples of how to estimate or calculate the wholesale cost of products that have been defined as OTP effective April 1, 2017. The CDTFA anticipates that proposed Regulation 4077 will promote fairness and benefit taxpayers and the CDTFA by defining the term “tobacco product manufacturer,” and clarifying who is regarded as the manufacturer of an electronic cigarette produced by mixing liquid nicotine with flavoring to make a customized product. The CDTFA also anticipates that the proposed amendments to Regulation 4076 and proposed Regulation 4077 will promote fairness and benefit taxpayers and the CDTFA by clarifying that OTP may only be distributed once, clarifying that a retailer does not make a taxable distribution by repackaging tax-paid OTP with other items for retail sale or selling tax-paid OTP with other items for a single price at retail, and clarifying that a retailer who is not a licensed manufacturer or distributor must purchase its nicotine products from a licensed tobacco products distributor or wholesaler.

In addition, the CDTFA has performed an evaluation of whether the proposed amendments to Regulation 4076 and proposed Regulation 4077 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments and proposed regulation are not inconsistent or incompatible with existing state regulations. This is because Regulation 4076 is the only regulation that clarifies the meaning of the phrase “wholesale cost” for purposes of the CTPTL and Regulation 4077 is the only regulation that clarifies who is a tobacco product manufacturer for purposes of the CTPTL. In addition, the CDTFA has determined that the provisions in the first sentence of proposed Regulation 4077 are comparable to the provisions in section 387(20)(A) of title 21 of the United States Code and do not substantially differ from the provisions in the federal statute, and that there are no comparable federal regulations or statutes to the amendments to Regulation 4076 or the other provisions in proposed Regulation 4077.

NO MANDATE ON LOCAL AGENCIES AND SCHOOL DISTRICTS

The CDTFA has determined that the adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 will not impose a mandate on local agencies or school districts, including a mandate that requires state reimbursement under part 7 (commencing with section 17500) of division 4 of title 2 of the Government Code.

ONE-TIME COST TO AND NON-QUANTITATIVE SAVINGS FOR THE CDTFA, BUT NO OTHER COST OR SAVINGS TO STATE AGENCIES, LOCAL AGENCIES, AND SCHOOL DISTRICTS

The CDTFA has determined that the adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 will result in an absorbable \$436 one-time cost for the CDTFA to update its website after the proposed regulatory action is completed. The CDTFA has also determined that the proposed amendments to Regulation 4076 are likely to produce some savings for the CDTFA by reducing the time it takes to perform audits, the number of times distributors will need to be billed for unreported or underreported taxes on electronic cigarettes, and the number of appeals. The CDTFA has determined that proposed Regulation 4077 is likely to produce some savings for the CDTFA by reducing the need for enforcement actions against unlicensed manufacturers. However, the CDTFA cannot quantitatively determine the amount of the savings.

In addition, the CDTFA has determined that the adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 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 Government Code, no other non-discretionary cost or savings imposed on local agencies, and no cost or savings in federal funding to the State of California.

NO SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS

The CDTFA has made an initial determination that the adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 will not have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

The adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 may affect small business.

NO MEASURABLE COST IMPACTS TO PRIVATE PERSONS OR BUSINESSES

The CDTFA is not aware of any direct cost impacts that a representative private person would necessarily incur in reasonable compliance with the proposed action.

The CDTFA has determined that the amendments to Regulation 4076 will have some direct impact on distributors of liquid nicotine products and accessories by clarifying when devices or delivery systems and any component, part, or accessory of such a device is sold in combination with nicotine and subject to tax as an electronic cigarette, which is included in the statutory definition of tobacco products, and some of the impacted distributors may be small businesses. Also, tobacco products taxes are generally passed onto wholesalers, retailers, and consumers in the form of higher prices. Therefore, the CDTFA has determined that the amendments to Regulation 4076 may have some indirect impact on wholesalers, retailers, and consumers if they increase the wholesale or retail price of devices, components, parts, or accessories that were classified as taxable electronic cigarettes at the time they were distributed, and some of the wholesalers and retailers may be small businesses. However, the amendments to Regulation 4076 do not require distributors to sell their devices, components, parts, or accessories in combination with nicotine, and they do not prevent distributors from changing their business

practices so that their sales of devices, components, parts, and accessories are not sales of electronic cigarettes subject to tax. Therefore, the CDTFA does not expect the amendments to measurably increase or decrease the taxes on or the wholesale or retail prices of devices, components, parts, and accessories or have a measurable cost impact on private persons or businesses.

The CDTFA has also determined that proposed Regulation 4077 will have some impact on businesses that manufacture tobacco products, including liquid nicotine products, in this state, and some of those businesses may be small business. This is because tobacco products manufacturers are required to register with the CDTFA for a Cigarette and/or Tobacco Products Manufacturer/Importer's License and some businesses may determine that they are manufacturers as a result of the regulation and incur costs to register with the CDTFA for a manufacturer's license that might be indirectly related to the proposed regulation. However, the CDTFA has determined that those indirect costs are likely to be relatively small and cannot be reliably estimated.

RESULTS OF THE ECONOMIC IMPACT ASSESSMENT REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b)

The CDTFA assessed the economic impact of the proposed amendments to Regulation 4076 and proposed Regulation 4077 on California businesses and individuals and determined that the proposed regulatory action is not a major regulation, as defined in Government Code section 11342.548 and California Code of Regulations, title 1, section 2000. Therefore, the CDTFA has prepared the economic impact assessment (EIA) required by Government Code section 11346.3, subdivision (b)(1), and included it in the initial statement of reasons. In the EIA, the CDTFA determined that the adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 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 in the state, and will not affect the expansion of businesses currently doing business in the State of California. Furthermore, the CDTFA determined that the adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 will not affect the benefits of the regulations to the health and welfare of California residents, worker safety, or the state's environment.

NO SIGNIFICANT EFFECT ON HOUSING COSTS

The adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077 will not have a significant effect on housing costs.

DETERMINATION REGARDING ALTERNATIVES

The CDTFA must determine that no reasonable alternative considered by it or that has otherwise been identified and brought to its attention would be more effective in carrying out the purpose 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.

CONTACT PERSONS

Questions regarding the substance of the proposed amendments to Regulation 4076 and proposed Regulation 4077 should be directed to Joshua Aldrich, Tax Counsel, by telephone at (916) 322-3283, by e-mail at Joshua.Aldrich@cdtfa.ca.gov, or by mail at California Department of Tax and Fee Administration, Attn: Joshua Aldrich, MIC:82, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0082.

Written comments for the CDTFA's consideration, written requests to hold a public hearing, notices of intent to present testimony or witnesses at the public hearing, and other inquiries concerning the proposed administrative action should be directed to Mr. Rick Bennion, Regulations Coordinator, by telephone at (916) 445-2130, by fax at (916) 322-2958, by e-mail at Richard.Bennion@cdtfa.ca.gov, or by mail at California Department of Tax and Fee Administration, Attn: Rick Bennion, MIC:50, 450 N Street, P.O. Box 942879, Sacramento, CA 94279-0050. Mr. Bennion is the designated backup contact person to Mr. Aldrich.

WRITTEN COMMENT PERIOD

The written comment period ends at 11:59 pm (PDT) on September 30, 2019. The CDTFA will consider the statements, arguments, and/or contentions contained in written comments received by Mr. Rick Bennion at the postal address, email address, or fax number provided above, prior to the close of the written comment period, before the CDTFA decides whether to adopt the proposed amendments to Regulation 4076 and proposed Regulation 4077. The CDTFA will only consider written comments received by that time.

However, if a public hearing is held, written comments may also be submitted at the public hearing and the CDTFA will consider the statements, arguments, and/or contentions contained in written comments submitted at the public hearing before the CDTFA decides whether to adopt the proposed amendments to Regulation 4076 and proposed Regulation 4077.

AVAILABILITY OF INITIAL STATEMENT OF REASONS AND TEXT OF PROPOSED REGULATION

The CDTFA has prepared a copy of the text of the proposed amendments to Regulation 4076 illustrating its express terms. The proposed amendments are illustrated in underline and strikeout format because California Code of Regulations, title 1, section 8, subdivision (b) provides that "the final text of the regulation shall use underline or italic to accurately indicate additions to, and strikeout to accurately indicate deletions from, the California Code of Regulations."

The CDTFA has prepared a copy of the text of proposed Regulation 4077 illustrating its express terms; however, the proposed regulation is not illustrated in underline or italics format because California Code of Regulations, title 1, section 8, subdivision (b) provides that "[u]nderline or italic is not required for the adoption of a new regulation or set of regulations if the final text otherwise clearly indicates that all of the final text submitted to OAL for filing is added to the California Code of Regulations."

The CDTFA has also prepared an initial statement of reasons for the adoption of the proposed amendments to Regulation 4076 and proposed Regulation 4077, which includes the economic impact assessment required by Government Code section 11346.3, subdivision (b)(1). These documents and all the information on which the proposed amendments and proposed regulation

are based are available to the public upon request. The rulemaking file is available for public inspection at 450 N Street, Sacramento, California. The express terms of the proposed amendments to Regulation 4076 and proposed Regulation 4077 and the initial statement of reasons are also available on the CDTFA's website at www.cdtfa.ca.gov.

PUBLIC HEARING

The CDTFA has not scheduled a public hearing to discuss the proposed amendments to Regulation 4076 and proposed Regulation 4077. However, any interested person or his or her authorized representative may submit a written request for an oral hearing no later than 15 days before the close of the written comment period, and the CDTFA will hold a public hearing if it receives a timely written request.

SUBSTANTIALLY RELATED CHANGES PURSUANT TO GOVERNMENT CODE SECTION 11346.8

The CDTFA may adopt the proposed amendments to Regulation 4076 and adopt proposed Regulation 4077 with changes that are non-substantial or solely grammatical in nature, or sufficiently related to the original proposed text that the public was adequately placed on notice that the changes could result from the originally proposed regulatory action. If a sufficiently related change is made, the CDTFA will make the full text of the proposed regulation, with the change clearly indicated, available to the public for at least 15 days before adoption. The text of the resulting regulation will be mailed to those interested parties who commented on the original proposed regulation orally or in writing or who asked to be informed of such changes. The text of the resulting regulation will also be available to the public from Mr. Bennion. The CDTFA will consider written comments on the resulting regulation that are received prior to adoption.

AVAILABILITY OF FINAL STATEMENT OF REASONS

If the CDTFA adopts the proposed amendments to Regulation 4076 and proposed Regulation 4077, the CDTFA will prepare a final statement of reasons, which will be made available for inspection at 450 N Street, Sacramento, California, and available on the CDTFA's website at www.cdtfa.ca.gov.