



# Special Notice

---

STATE BOARD  
OF  
EQUALIZATION

450 N Street  
Sacramento  
California 95814

**BOARD MEMBERS**

CAROLE MIGDEN  
First District  
San Francisco

BILL LEONARD  
Second District  
Ontario

CLAUDE PARRISH  
Third District  
Long Beach

JOHN CHIANG  
Fourth District  
Los Angeles

STEVE WESTLY  
State Controller  
Sacramento

**INTERIM EXECUTIVE  
DIRECTOR**

Timothy W. Boyer  
Sacramento

## Notice to Vehicle Manufacturers, Distributors and Dealers

### Update on Handling Sales Tax Under the California “Lemon Law”

#### General

This notice is effective immediately and supersedes all prior notices for handling “Lemon Law” transactions. The “Lemon Law” for new motor vehicles falls under sections 1793.2 through 1793.26 of the California Civil Code. The “Lemon Law” provides recourse to the customer when a vehicle is not repaired to conform to the applicable express warranties after a reasonable number of attempts. The manufacturer must either reimburse the customer (make restitution) for the adjusted cost of the original vehicle including sales tax reimbursement, or replace the vehicle. The customer may select monetary restitution or vehicle replacement.

The “Lemon Law” provides that manufacturers may receive reimbursement from the Board of Equalization for sales tax reimbursement refunded to customers. *This special notice provides updated procedures on the handling of “Lemon Law” transactions involving replacement vehicles.* The former **Alternative Method**, described in Audit Manual 0616.25 (July 2000), in which treating vehicle replacements as two separate transactions, is no longer acceptable.

#### When The Customer Selects Restitution

The manufacturer must pay an amount equal to the actual price paid or payable by the customer, including any sales tax, license fees, registration fees, and other official fees, plus any incidental damages to which the buyer is entitled. The manufacturer may deduct amounts for the usage of the defective vehicle and any amount charged for non-manufacturer items installed by the dealer from the original vehicle selling price before calculating the sales tax refund. See the sample claim for refund calculation in *Example 1* of the Appendix.

#### When The Customer Selects Vehicle Replacement

Most “Lemon Law” transactions involving replacement vehicles are coordinated by manufacturers through their dealerships. The updated Board procedures pertain to vehicle replacement. When a customer chooses

November 2003

replacement, the replacement vehicle is considered a single transaction under a mandatory warranty. When manufacturers adhere to this provision, they should only file a claim for refund when the value of the replacement vehicle is less than the original vehicle and the customer has been refunded the difference, including applicable sales tax reimbursement.

The following examples outline the acceptable procedures to follow for vehicle replacements:

1. **The customer selects a replacement vehicle having a value greater than the credit given for the original vehicle.** In this situation, the dealership is liable for the sales tax on the amount the customer pays in excess of the credit given for the original vehicle (the incremental amount). License (registration) and amounts billed for non-taxable fees included in the credit given for the original vehicle should not be deducted from the price of the new vehicle when calculating the amount subject to tax. The dealership must report only the *incremental amount* (the difference between the replacement vehicle and the credit allowed for the original vehicle) on its sales and use tax return as a taxable sale, rather than the full amount of the sales price of the replacement vehicle. See the sample calculation of sales tax due in *Example 2* of the Appendix.
2. **The customer selects a replacement vehicle having a value less than the credit given for the original vehicle.** The manufacturer should refund the difference to the customer, including sales tax reimbursement. The manufacturer may seek a refund of sales tax included in the amount reimbursed to the buyer by filing a claim for refund with the Board. The dealership should not report this replacement transaction on its sales and use tax return. See the sample claim for refund calculation in *Example 3* of the Appendix.
3. **The customer selects a replacement vehicle with an equivalent price and an exchange of vehicles occurs at no additional cost.** Since the credit for the returned vehicle is the same as the negotiated sales price of the replacement vehicle and no additional amount is required to be paid, the transaction should not be reported on the dealer’s sales and use tax return. The manufacturer should not file a claim for refund for the sales tax on the original vehicle.

### Supporting Documentation Required

Vehicle dealers with “Lemon Law” replacement transactions must retain documentation in their files explaining and supporting these transactions. The dealership must retain any documentation provided by the manufacturer and make it available upon request by the Board in support of the transactions and any claims for refund filed by the manufacturer.

To support the transaction, the dealer must retain, at a minimum, the original sales contract, the new sales contract (if applicable), and any documentation provided by the manufacturer. In addition, the dealer must retain an explanation of how any credits allowed the buyer were calculated including the amount of sales tax reimbursement included in the credit to the buyer.

### **Filing A Claim For Refund**

If the manufacturer, through their authorized dealership, is unable to restore the vehicle to mandatory warranty conformity, the dealership can be authorized by the manufacturer to handle the transaction as a "Lemon Law" transaction. The customer has the option to select either a monetary restitution or vehicle replacement. The manufacturer may file a claim for refund of the tax with the Board when either:

1. full monetary restitution is made to the customer, or
2. the customer selects a replacement vehicle having a value less than the original vehicle and the difference (including sales tax reimbursement) is refunded to the buyer.

The claim for refund must state that restitution was paid to the customer in accordance with sections 1793.2 through 1793.26 of the California Civil Code. A copy of all documentation regarding the transaction should accompany the claim, including the amount of sales tax reimbursement refunded or credited, a copy of the branded title of the reacquired vehicle (with the notation "LEMON LAW BUYBACK"), and copies of documents to support the amount refunded to the customer. In addition, a statement must be submitted from the dealership which originally sold the vehicle to indicate sales tax was reported on the original sales transaction.

All claims should be sent to the following address:

California State Board of Equalization  
Audit Determination and Refund Section, MIC 39  
PO Box 942879  
Sacramento, CA 94279-0039

A list of Board of Equalization offices and their telephone numbers is included with this notice. If you have any questions, please call the office nearest you or the Taxpayer Information Center at 800-400-7115.

## Appendix

**Example 1: Restitution -- Method of calculating sales tax refund when the customer elects restitution in lieu of replacement.**

The tax rate in effect at the time of purchase was 8.25%. The vehicle was driven 5,907 miles prior to the first nonconformity. Please note, this example does not take into account other types of manufacturer to customer reimbursements (e.g., finance charges, attorney fees, rental car, etc.)

<u>Description</u>	<u>Per Sales Contract (Original Vehicle)</u>
A. Cash Price of Vehicle	\$22,100.00
B. Accessories	
1. Manufacturers Installed Options	\$500.00
2. Dealer Installed Options	\$150.00
C. Document Fee	\$ 45.00
<b>Less: Usage *</b>	(\$1,112.49)
Dealer Installed Options **	(\$150.00)
<i>Subtotal</i>	\$21,532.51
D. Sales Tax Refund (\$21,532.51 X 8.25%)	<b>\$ 1,776.43</b>
E. License Fee	\$183.00
<b>Total</b>	<b>\$23,491.94</b>

In the above case, the manufacturer is required to reimburse the customer a minimum of **\$23,491.94** as restitution. When the customer is fully reimbursed and all other applicable requirements of the Civil Code are met, the manufacturer may file a claim for refund with the Board of Equalization for the sales tax in the amount of \$1,776.43.

**\* Usage Calculation** – The customer is liable for use of the defective vehicle prior to the time the customer first delivers the vehicle to the manufacturer, or to its authorized service and repair facility for correction of the problem that gave rise to the nonconformity. The amount attributable to such use by the customer will be calculated by multiplying the total sales price of the motor vehicle by a fraction having as its denominator 120,000 and as its numerator the number of miles the vehicle was used by the customer, up to the first nonconformity.

Cash Price of Original Vehicle	X	<u>Miles Driven Prior to the First Nonconformity</u>		
		120,000		
( \$22,100 + \$500 )	X	<u>5,907</u>	=	<u>\$1,112.49</u>
		120,000		

**\*\* Dealer installed options are not required to be reimbursed under the Civil Code.**

**Appendix (continued)**

**Example 2: Replacement Vehicle -- Method of calculating sales tax due when the replacement vehicle has a value greater than the credit given for the original vehicle.**

The tax rate of 8.25% was in effect at the time of both transactions, the replacement and the original purchase. The original vehicle was driven 5,907 miles prior to the first nonconformity. This example does not take into account other types of manufacturer to customer reimbursements (e.g., finance charges, attorney fees, rental car, etc.)

<u>Description</u>	<u>Replacement Vehicle (Negotiated Price)</u>	<u>Per Sales Contract (Original Vehicle)</u>	<u>Difference</u>
A. Cash Price of Vehicle	\$28,500.00	\$22,100.00	\$6,400.00
B. Accessories			
1. Manufacturers Installed Options	\$855.00	\$500.00	\$355.00
2. Dealer Installed Options	\$200.00	\$150.00	\$50.00
C. Document Fee	\$45.00	\$45.00	\$0.00
<b>Less:</b> Usage *		(\$1,112.49)	\$1,112.49
Dealer Installed Options**		(\$150.00)	\$150.00
<b>Subtotal</b>	<b>\$29,600.00</b>	<b>\$21,532.51</b>	<b>\$8,067.49</b>
D. Sales Tax Due (\$8,067.49 x 8.25%)	\$665.57		\$665.57
E. License Fee	\$237.00	\$183.00	\$54.00
<b>Total</b>	<b>\$30,502.57</b>	<b>\$21,715.51</b>	<b>\$8,787.06</b>

In the above case, the customer is entitled to a total credit of \$21,715.51 from the original sales contract. Since the value of the replacement vehicle was greater than the original vehicle the customer would owe additional sales tax of \$665.57 on the additional taxable measure of \$8,067.49. The additional taxable measure of \$8,067.49 should be reported to the Board of Equalization along with the additional sales tax due of \$665.57 for the replacement vehicle for the period in which the replacement transaction takes place. Therefore, the manufacturer should not file a claim for refund on this transaction. The customer is responsible for paying the additional amount of \$8,787.06 to cover the additional cost of the replacement vehicle. The total allowable credit from the original vehicle applied towards the replacement vehicle is \$21,715.51.

\* **Usage Calculation** – The customer is liable for use of the defective vehicle prior to the time the customer first delivers the vehicle to the manufacturer, or to its authorized service and repair facility for correction of the problem that gave rise to the nonconformity. The amount attributable to such use by the customer will be calculated by multiplying the total sales price of the motor vehicle by a fraction having as its denominator 120,000 and as its numerator the number of miles the vehicle was used by the customer, up to the first nonconformity.

$$\begin{array}{rcl}
 \text{Cash Price of Original Vehicle} & \times & \frac{\text{Miles Driven Prior to the First Nonconformity}}{120,000} \\
 \\ 
 (\$22,100 + \$500) & \times & \frac{5,907}{120,000} = \underline{\underline{\$1,112.49}}
 \end{array}$$

\*\* Dealer installed options are not required to be reimbursed under the Civil Code.

### Appendix - Continued

**Example 3. Replacement Vehicle -- Method of calculating the sales tax refund when the replacement vehicle has a value less than the credit given for the original vehicle.**

The tax rate of 8.25% was in effect at the time of both transactions, the replacement and the original purchase. The original vehicle was driven 5,907 miles prior to the first nonconformity. This example does not take into account other types of manufacturer to customer reimbursements (e.g., finance charges, attorney fees, rental car, etc.)

<u>Description</u>	<u>Replacement vehicle (Negotiated Price)</u>	<u>Per Sales Contract (Original Vehicle)</u>	<u>Difference</u>
A.Cash Price of Vehicle	\$15,700.00	\$22,100.00	(\$6,400.00)
B. Accessories			
1. Manufacturers Installed Options	\$145.00	\$500.00	(\$355.00)
2. Dealer Installed Options	\$100.00	\$150.00	(\$50.00)
C.Document Fee	\$45.00	\$45.00	\$0.00
<b>Less: Usage *</b>		(\$1,112.49)	\$1,112.49
Dealer Installed Options**		(\$150.00)	\$150.00
<b>Subtotal</b>	<b>\$15,990.00</b>	<b>\$21,532.51</b>	<b>(\$5,542.51)</b>
D.Sales Tax Refund (\$5,542.51 X 8.25%)		\$457.26	<b>(\$457.26)</b>
E.License Fees	\$130.00	\$183.00	(\$53.00)
<b>Total</b>	<b>\$16,120.00</b>	<b>\$22,172.77</b>	<b>(\$6,052.77)</b>

In the above case, the customer is entitled to a **\$6,052.77** refund directly from the manufacturer as well as the replacement vehicle costing **\$16,120.00** for a total credit amounting to **\$22,172.77**. When the customer is fully reimbursed and all other requirements of the Civil Code are met, the manufacturer may file a claim for refund with the Board of Equalization for **\$457.26** in sales tax reimbursed.

**\* Usage Calculation** – The customer is liable for use of the defective vehicle prior to the time the customer first delivers the vehicle to the manufacturer, or to its authorized service and repair facility for correction of the problem that gave rise to the nonconformity. The amount attributable to such use by the customer will be calculated by multiplying the total sales price of the motor vehicle by a fraction having as its denominator 120,000 and as its numerator the number of miles the vehicle was used by the customer, up to the first nonconformity.

$$\begin{array}{rcl}
 \text{Cash Price of Original Vehicle} & \times & \frac{\text{Miles Driven Prior to the First Nonconformity}}{120,000} \\
 (\$22,100 + \$500) & \times & \frac{5,907}{120,000} = \underline{\$1,112.49}
 \end{array}$$

**\*\* Dealer installed options are not required to be reimbursed under the Civil Code.**

**CALIFORNIA STATE BOARD OF EQUALIZATION**

**Field Office Locations and Addresses**

**HEADQUARTERS**

**Sacramento** **PO Box 942879, 94279-0001** **800 400-7115**

CALIFORNIA CITIES	OFFICE ADDRESS	AREA TELEPHONE CODE NUMBER
Bakersfield	1800 30th Street, Suite 380, 93301-1922 (PO Box 1728, 93302-1728)	661 395-2880
Culver City	5901 Green Valley Circle, Suite 200, 90230-6948 (PO Box 3652, 90231-3652)	310 342-1000
El Centro	1550 W. Main Street, 92243-2832 <b>Note:</b> closed 12 noon to 1 p.m. M-F	760 352-3431
Eureka	134 D Street, Suite 301, 95501-0455 (PO Box 4884, 95502-4884) <b>Note:</b> closed 12 noon to 1 p.m. M-F	707 445-6500
Fresno	5070 N. Sixth Street, Suite 110, 93710-7504 (PO Box 28580, 93729-8580)	559 248-4219
Kearny Mesa	9225 Clairemont Mesa Boulevard, San Diego, CA 92123 <b>Note:</b> closed 12 noon to 1 p.m. M-F	858 636-3191
Laguna Hills	23141 Moulton Parkway, Suite 100, 92653-1242	949 461-5711
Long Beach	100 West Broadway, Suite 305, 90802-4431	562 901-2483
Norwalk	12440 E. Imperial Highway, Suite 201, 90650-8397 (PO Box 409, 90651-0409)	562 466-1694
Oakland	1515 Clay Street, Suite 303, 94612-1432	510 622-4100
Rancho Mirage	42-700 Bob Hope Drive, Suite 301, 92270-7167	760 346-8096
Redding	2881 Churn Creek Road, Suite B, 96002-1146 (PO Box 492529, 96049-2529)	530 224-4729
Riverside	3737 Main Street, Suite 1000, 92501-3395	909 680-6400
Sacramento	3321 Power Inn Road, Suite 210, 95826-3889	916 227-6700
Salinas	111 East Navajo Drive, Suite 100, 93906-2452	831 443-3003
San Diego	1350 Front Street, Rm 5047, 92101-3698	619 525-4526
San Francisco	121 Spear Street, Suite 460, 94105-1584	415 356-6600
San Jose	250 South Second Street, 95113-2706	408 277-1231
San Marcos	334 Via Vera Cruz, Suite 107, 92069-2694	760 510-5850
Santa Ana	28 Civic Center Plaza, Rm 239, 92701-4011	714 558-4059
Santa Rosa	50 D Street, Rm 230, 95404-4791 (PO Box 730, 95402-0730)	707 576-2100
Stockton	31 East Channel Street, Rm 264, 95202-2314 (PO Box 1890, 95201-1890)	209 948-7720
Suisun City	333 Sunset Avenue, Suite 330, 94585-2003	707 428-2041
Torrance	680 W. Knox Street, Suite 200, 90502-1358 (PO Box T, 90508-0270)	310 516-4300
Van Nuys	15350 Sherman Way, Suite 250, 91406-4203 (PO Box 7735, 91409-7735)	818 904-2300
Ventura	4820 McGrath Street, Suite 260, 93003-777	805 677-2700
West Covina	1521 West Cameron Ave., Suite 300, 91790-2738 (PO Box 1500, 91793-1500)	626 480-7200

**OUT-OF-STATE FIELD OFFICES**

Sacramento	3321 Power Inn Road, Suite 130, 95826-3893 (PO Box 188268, 95818-8268)	916 227-6600
Chicago, Illinois	120 N. La Salle, Suite 1600, 60602-2412	312 201-5300
New York, N.Y.	205 East 42nd Street, Suite 1100, 10017-5706	212 697-4680
Houston, Texas	1155 Dairy Ashford, Suite 550, 77079-3007	281 531-3450

**TDD INFORMATION**

California Relay Telephone Service for the Deaf and Hearing Impaired - From TDD telephones dial 800-735-2929; from voice-operated telephones dial 800-735-2922.

Addresses and telephone numbers are current as of **9-22-03**, but are subject to change. We recommend you call the office before visiting.

**Unless otherwise noted all offices are open from 8 a.m. to 5 p.m. Monday-Friday, excluding state holidays.**