

**Amend Section 6248 of the Revenue and Taxation Code to reinstate the provisions for a 12-month test applied to out-of-state purchases of vehicles, vessels, and aircraft, which expired on June 30, 2007 and to clarify its provisions related to the definition of “California resident” and the exception for repair, retrofit, and modification.**

**Source: Sales and Use Tax Department**

### **Existing Law**

The approval of the 2004-2005 California Budget included SB 1100 (Stats 2004, Chapter 226), which in part amended Revenue and Taxation Code Section 6248. The amendments replaced the “90-day test” for determining if the out-of-state purchase of a vehicle, vessel, or aircraft is for the purpose of storage, use, or other consumption in California and subject to California use tax with a “12-month test” for the period from October 2, 2004, to June 30, 2006. AB 1809 (Stats 2006, Chapter 49) extended the sunset date for the 12-month test until June 30, 2007.

During the period from October 2, 2004, through June 30, 2007, any vehicle, vessel, or aircraft purchased outside of California and brought into California within 12 months from the date of its purchase was presumed to be acquired for storage, use, or other consumption in California and subject to tax if any of the following occurred:

1. The vehicle, vessel, or aircraft was purchased by a California resident as defined in Section 516 of the California Vehicle Code, **or**
2. In the case of a vehicle, the vehicle was subject to vehicle registration in California during the first twelve months of ownership, **or**
3. In the case of an aircraft or vessel, the aircraft or vessel was subject to property tax in California during the first twelve months of ownership, **or**
4. The vehicle, vessel, or aircraft is used or stored in this state more than one-half of the time during the first 12 months of ownership.

### **Background**

When Section 6248 of the Revenue and Taxation Code was amended to provide a “12-month test,” it became more difficult for California residents to demonstrate that a vehicle, vessel, or aircraft was purchased for use outside of California, and successfully avoid both California taxes and other states’ taxes. Consideration of residency and registration as factors in determining the applicability of the use tax to out-of-state purchases (rather than simply a test of time and location) closed what many perceived to be a loophole. According to an April 2006 report by the Legislative Analyst’s Office, the change to the 12-month test resulted in a sharp decline in exemptions for purchases of yachts and recreational vehicles (RV’s) for use out of state and an increase in sales and use tax revenues of approximately \$45 million per year.

However, news articles described another scheme for avoiding tax on purchases of RV’s as a loophole that became more common with the introduction of the 12-month test. For example, an article in the September 25, 2006, issue of the Los Angeles Times, “*Under A Big Sky, They Turn RVs Into Dodges*,” reports:

*Montana has no sales tax, and recreational-vehicle aficionados are taking a break from their road maps and AAA Trip-Tiks to set up shell corporations in the state...Most states make it difficult for nonresidents to get license plates. But Montana lets out-of-staters register vehicles if they own a local limited liability corporation. Setting one up merely requires some simple paperwork and about \$1300 to cover incorporation costs, registration fees and attorney hours.*

By setting up a limited liability company (LLC) in Montana to own an RV, California residents not only can take advantage of Montana's lower vehicle registration fees, but when they bring their RV's into California, assuming that the 12-month test is reinstated, they may believe that their purchases are not subject to the same presumptions regarding whether or not the vehicles were purchased for use in California as vehicle purchases by other California residents.

Information recently received by the Board shows approximately 900 vehicles registered in Montana by Montana LLC's that appear to be closely held by California residents. Estimated taxable measure for these 900 vehicles is \$227 million with tax of \$16.5 million. The Los Angeles Times article, *Under a Big Sky...*, reports that based on comparisons of Montana vehicle records with California addresses, officials at the California Attorney General's office say they believe as many as 10,000 Californians have put Montana plates on their motor homes in recent years, costing the State over \$160 million for "this particular type of fraud."

For vessel purchases, it appears that many California residents are establishing LLC's or corporations in Oregon to show an Oregon address for their vessels. The Board's Consumer Use Tax Section has identified a recurring Oregon address for the agent of record claiming exemption for transfers of vessels to a commencing corporation. The Oregon Secretary of State's database shows 973 transfers registered in Oregon by this agent as of 10/08/07. Of those, 244 have been identified as LLC's connected to California through the address identified as the principal place of business, the mailing address, or the address for the members.

### **This Proposal**

Since an LLC registered in Montana or a closely-held corporation established in Oregon may not appear to fall within the definition of a California resident under Section 6248 as it was written previously, there could be confusion as to whether an RV purchased by an LLC is subject to the same presumptions as vehicles purchased by other residents of California. To close this perceived loophole and clarify the presumptions that apply to an out-of-state purchase of a vehicle, vessel, or aircraft by a corporation or an LLC, this proposal would revise the definition of "California resident" to include a closely-held corporation or LLC if 50 percent or more of the shares or membership interests are held by shareholders or members who are California residents. With this expanded definition, it would be clear that the presumptions about whether or not a vehicle, vessel, or aircraft was purchased for use in California would be the same for all California residents, whether or not they set up a corporation or an LLC in Montana, Oregon, or any other state for ownership of the vehicle, vessel, or aircraft.

A second "loophole" in the provisions of Section 6248 that were operative from October 2, 2004, through June 30, 2007, was the exception for "repair, retrofit, and modification" (RR&M). This exception was included in law so that California businesses that service vessels and aircraft would not be harmed economically. The abuses of this exception with aircraft were minor, since aircraft RR&M is required by the FAA to be performed or inspected by an FAA certified repair facility. However, this exception was widely abused by vessel owners. Many vessel owners were constantly changing or repairing items on their vessels, and many vessels in California were used regularly without leaving their moorage. Thus, the Board has had many cases where a taxpayer regularly purchased minor parts or accessories for self-performed RR&M over an extended period of time without ever sailing the vessel, and while keeping and using the vessel in California for purposes other than sailing. In one case, a taxpayer even lived on board the vessel while self-performing RR&M; but asserted that since the vessel was not sailed for more than 25 hours, the vessel was not taxable under the law.

This proposal would therefore clarify that repairs, retrofit, and modification will only qualify for the exception to the 12-month test if they are performed by a properly certified and/or licensed and permitized repair facility. The proposed change preserves the legislative desire to minimize the impact of the 12-month test on California businesses in the industry, while clarifying that the exception was not provided as a method of tax avoidance.

*Section 6248 of the Revenue and Taxation Code is amended to read:*

6248. (a) ~~On and after July 1, 2007, there~~ There shall be a rebuttable presumption that any vehicle, vessel, or aircraft bought outside of this state, and which is brought

into California within ~~90 days~~ 12 months from the date of its purchase, ~~and which is subject to registration under Chapter 1 (commencing with Section 4000) of Division 3 of the Vehicle Code,~~ was acquired for storage, use, or other consumption in this state and is subject to use tax if any of the following occur:

(1) The vehicle, vessel, or aircraft was purchased by a California resident as defined in Section 516 of the Vehicle Code. For purposes of this paragraph, a closely-held corporation or limited liability corporation shall be regarded as a California resident when fifty percent or more of the shares or membership interests are held by shareholders or members who are California residents as defined in Section 516 of the Vehicle Code.

(2) In the case of a vehicle, the vehicle was subject to registration under Chapter 1 (commencing with Section 4000) of Division 3 of the Vehicle Code during the first 12 months of ownership.

(3) In the case of a vessel or aircraft, that vessel or aircraft was subject to property tax in this state during the first 12 months of ownership.

(4) If purchased by a non-resident of California, the vehicle, vessel, or aircraft is used or stored in this state more than one-half of the time during the first 12 months of ownership.

(b) This presumption may be controverted by documentary evidence that the vehicle, vessel, or aircraft was purchased for use outside of this state during the first 12 months of ownership. This evidence may include, but is not limited to, evidence of registration of that vehicle, vessel, or aircraft, with the proper authority, outside of this state.

(c) This section does not apply to any vehicle, vessel, or aircraft used in interstate or foreign commerce pursuant to regulations prescribed by the board.

(d) The amendments made to this section by the act adding this subdivision do not apply to any vehicle, vessel, or aircraft that is either purchased, or is the subject of a binding purchase contract that is entered into, on or before the operative date of this subdivision.

(e) Notwithstanding subdivision (a), an aircraft or vessel brought into this state exclusively for the purpose of repair, retrofit, or modification shall not be deemed to be acquired for storage, use, or other consumption in this state; provided such repair, retrofit, or modification is either of the following::

(1) In the case of an aircraft, performed by a repair station certified by the Federal Aviation Administration or a manufacturer's maintenance facility; or

(2) In the case of a vessel, performed by a repair facility that possesses a seller's permit and is licensed to do business by the city or county in which it is located.

(f) The presumption set forth in subdivision (a) may be controverted by documentary evidence that the vehicle was brought into this state for the exclusive purpose of warranty or repair service and was used or stored in this state for that purpose for 30 days or less. The 30-day period begins when the vehicle enters this state, includes any

time of travel to and from the warranty or repair facility, and ends when the vehicle is returned to a point outside the state. The documentary evidence shall include a work order stating the dates that the vehicle is in the possession of the warranty or repair facility and a statement by the owner of the vehicle specifying dates of travel to and from the warranty or repair facility.

(g) The amendments made to this section by this act shall apply to all purchases of vehicles, vessels, or aircraft occurring on or after the effective date of this section. ~~This section shall become operative on July 1, 2007.~~