In the Supreme Court of the State of California

MICHAEL McCLAIN, et al.,

Plaintiffs and Appellants,

v.

SAV-ON DRUGS, et al.,

Defendants and Respondents.

Case No. S241471

Second Appellate District, Div. Eight, Case Nos. B265011 and B265029
Los Angeles County Superior Court, Case Nos. BC325272 and BC327216
John Shepard Wiley, Judge

RESPONDENT CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION'S CONSOLIDATED ANSWER TO AMICUS CURIAE BRIEFS

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TABLE OF CONTENTS

TABLE OF CONTENTS
(continued)

Page

TABLE OF AUTHORITIES

Page

CASES

TABLE OF AUTHORITIES
(continued)

Page

STATUTES

TABLE OF AUTHORITIES
(continued)

Page

TABLE OF AUTHORITIES
(continued)

Page

INTRODUCTION AND SUMMARY

In this consolidated answer brief, defendant and respondent the California Department of Tax and Fee Administration responds to amici Alina Bekkerman, et. al.; Consumer Attorneys of California, et al.; Howard Jarvis Taxpayers Association, et al.; Larry Littlejohn; and Public Citizen, Inc. (collectively, amici). In the main, these amici repeat plaintiffs' arguments, which the Department fully addressed in its answer brief.[1]

As set out in the Department's answer and further discussed below, consumers have the ability to influence the content, interpretation, and application of sales tax exemptions through interactions with retailers, and through requests for discretionary action made to the Department, consistent with the tax code, or to the Legislature. (ABM 39-43.) But neither the tax code nor the state or federal Constitution confers on consumers the right to institute tax refund-related proceedings—a right which belongs only to retailers as taxpayers. (*Id.* at 18-20.) Creating such a right in the circumstances of this case would be both unworkable and unwise.

Allowing consumers to bring extra-statutory claims against the Department seeking a return of sales tax reimbursement paid, based on consumers' claims that retailers could have asserted sales tax exemptions, but did not do so, where the Department has not already determined that a tax refund is due under its normal statutory procedures (e.g., in the context of an audit, deficiency determination, or taxpayer refund action), would substantially expand the relief recognized in the "unique" circumstances of

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[1] The Department was not named in plaintiffs' breach-of-contract claim, and, therefore, continues to leave the briefing on the viability of this claim largely to the retailer defendants. (See Answer Brief on the Merits (ABM) 15, fn. 2; *id.* at 38, fn. 18.)

Javor v. State Bd. of Equalization (1974) 12 Cal.3d 790, 802. (ABM 30-34.) Such judicial expansion would work against the objectives of the tax code; interfere with the Legislature's constitutional prerogative to set tax policy; encourage extensive, complex, and costly litigation; and disrupt sales tax revenues essential to government operation. (ABM 34-39; see also Amicus Brief of League of California Cities and California State Assn. of Counties 10 [noting adverse effects to local government finance from broad ruling that would recognize a "refund remedy for those who bear the economic, but not legal, burden of a revenue measure"].)

Declining to expand consumer *Javor* remedies to allow consumers to file suit against retailers and the Department to dispute in the first instance the routine application of sales tax exemptions would not violate due process. (ABM 43-50.) Due process requires that *taxpayers* be afforded an opportunity to dispute the imposition of taxes. From the first iteration of the Retail Sales Act in the early 1930s, through reforming amendments in the late 1970s, the Legislature has been clear that retailers, not consumers, pay sales tax. While retailers may seek sales tax reimbursement from consumers by contract, only retailers are responsible for paying sales tax to the State. Accordingly, only taxpaying retailers may decide whether to meet any required conditions of, document, and assert particular sales tax exemptions, and whether to pay sales taxes under protest and file claims for refunds where the application of an exemption is unclear or disputed.

Under the system designed by the Legislature, the burdens of sales taxes, and the benefits of sales tax exemptions, fall on retailers as taxpayers, affecting consumers only indirectly. And it is well settled that the right to due process does not protect against the indirect adverse effects of governmental action. (ABM 49-50.) Federal cases addressing federal tax immunity cited by amici Bekkerman and Howard Jarvis do not require the Court to reject the state Legislature's express and unequivocal decision

to make retailers, not consumers, legally responsible for paying sales tax, and to provide only retailers with the type of concrete statutory interest that is constitutionally protected by the Due Process Clause.

The Department continues—within the limits of its authorizing statutes—to facilitate retailers' efforts to take advantage of the conditional sales tax exemption for glucose test strips and lancets that the Department itself created by regulation. If in the future the Legislature chooses to enact different or broader exemptions for these products, the Department will of course take appropriate action to implement and administer those policy decisions. But consumers' dissatisfaction with the extent, clarity, or administration of the existing statutory exemptions provides no ground for the courts to create new consumer remedies.

ARGUMENT

I. *JAVOR* SHOULD NOT BE EXTENDED TO ALLOW CONSUMERS TO PURSUE CLAIMS CHALLENGING RETAILERS' ROUTINE APPLICATIONS OF SALES TAX EXEMPTIONS

A. The Absence of a Statutory Refund Action for Consumers Is a Consequence of the Legislature's Decision That Retailers—Not Consumers—Are Taxpayers

The Department's answer brief detailed the ways in which it encourages retailers to claim sales tax exemptions for the benefit of consumers, and how consumers can both influence retailers, and request Department action related to such exemptions. In the latter category, consumers may, for example, petition the Department for a rulemaking to clarify a statutory exemption, request a Department audit of a retailer's sales tax exemption practices, or file a declaratory relief action challenging

a Department regulation as inconsistent with a statute or the Constitution.[2] (ABM 39-43; *Loeffler v. Target Corp.* (2014) 58 Cal.4th 1081, 1123.)[3] Amici express frustration with the limited nature of consumers' statutory options, which do not include consumer-initiated sales tax refund actions against the Department. (See Bekkerman 44-45; Howard Jarvis 12, 14-15, 16-17; Public Citizen 1-2, 5-7; see also Reply Brief on the Merits (RBM) 38-39.)[4] These limits are, however, the natural result of the Legislature's

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[2] The record does not reflect, and the Department is not aware, that plaintiffs or amici have taken any such actions related to the sales tax exemptions at issue in this case.

[3] When the Department ascertains by audit, in a deficiency determination, or in a refund action that a retailer has collected excess sales tax reimbursement, it can also order prospective relief—for example, that a retailer not collect sales tax reimbursement on certain future sales, and it can order the retailer to return any unremitted tax reimbursement to its customers. (Rev. & Tax. Code, §§ 6901.5, 7051 [Department "shall enforce" sales and use tax provisions]; *Loeffler, supra,* 58 Cal.4th at pp. 1118-1121 [discussing § 6901.5].) With respect to amounts that the retailer has remitted to the Department, the Department conditions any refund to the taxpaying retailer on the retailer's return of the excess reimbursement payments to the retailer's customers. (*Loeffler*, *supra*, 58 Cal.4th at p. 1117 [discussing *Decorative Carpets, Inc. v. State Bd. of Equalization* (1962) 58 Cal.2d 252, 254-255]; see also ABM 41; Cal. Code. Regs., tit. 18, § 1700 ["Reimbursement for Sales Tax"].)

[4] Public Citizen asserts that the Department has "an incentive" to "ignore a request to conduct an audit or deficiency determination" if the process "might result in a refund." (Public Citizen 6; see also Littlejohn 4, 6; Consumer Attorneys 6; RMB 39.) In fact, the Department's audit program "has resulted in the correction of tax underpayments *and overpayments* of many millions of dollars." (Audit Manual (Aug. 2007), ¶ 0101.20, italics added, available at <https://boe.ca.gov/sutax/manuals/fam-01.pdf> [as of July 10, 2018]; see also *id.* at ¶ 0101.03 [stated mission to "serve the public through fair, effective, and efficient tax administration"].) Indeed, the facts of this case show that the Department does not view its responsibility as simply maximizing tax revenues. The regulatory exemption for glucose test strips is an *extension* of the statutory

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decision to make retailers—not consumers—the taxpayers in retail sales transactions, and to restrict refund actions to taxpayers, as the Legislature is authorized to do. (See, e.g., Cal. Const., art. XIII, § 32 [authorizing post-payment action to recover illegal tax "in such manner as may be provided by the Legislature"]; *id.* at § 33 [authorizing Legislature to "pass all laws necessary to carry out" art. XIII, governing taxation]; Rev. & Tax. Code, § 6051 [providing that sales tax is "hereby imposed upon all retailers"]; § 6901 et seq. [setting out administrative procedure for taxpayer refund claims]; *National Ice & Cold Storage Co. v. Cal. Pacific Fruit Express Co.* (1938) 11 Cal.2d 283, 289-290; ABM 15-21 [summarizing sales tax law and observing that the retailer is the taxpayer]; *Loeffler, supra,* 58 Cal.4th at pp. 1101-1104 [same].)[5]

B. The Unique Circumstances of *Javor*, Which Caused the Court to Recognize an Extra-statutory Consumer Claim, Are Not Present Here

To avoid this result, amici argue that the limited, extra-statutory claim recognized by this Court in *Javor* should be broadly available to allow consumers to challenge retailers' routine application of sales tax exemptions and to seek refunds of sales tax reimbursement for completed transactions. For legal and practical reasons, the Court should decline to extend *Javor* that far.

In *Javor*, the Court held that a class of automobile purchasers was entitled to bring an action against auto retailers for a refund of sales tax reimbursement, and to join the Board of Equalization (the predecessor

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exemption for prescription medicines, and, as an exemption, necessarily operates to reduce tax revenues. (See ABM 21-23.)

[5] All further references are to the Revenue and Taxation Code unless otherwise specified.

agency to the Department) to that suit. (*Javor*, *supra*, 12 Cal.3d at p. 802; see also ABM 30-33 [summarizing *Javor*].) In *Javor*, a post-sale change in federal law reduced the federal excise tax on certain vehicles that had been sold in California. (*Javor*, *supra*, 12 Cal.3d at p. 794.) The agency interpreted that change in federal law to have effected under state law a retroactive reduction in the vehicles' sales price on which state sales tax had been calculated. (*Ibid.*) The agency then implemented the law by promulgating a rule recognizing a retroactive sales price adjustment caused by a change in federal law, which in turn reduced the sales tax that auto retailers owed to the State. (*Ibid.*) The regulation further provided that excess sales tax would be refunded to affected retailers, provided retailers repaid to consumers any associated excess sales tax reimbursement. (*Ibid.*) The regulation was supplemented by a "notification and 'operations memo'" to dealers and interested parties and a "news release" informing consumers that they could demand and receive refunds from dealers. (*Id.* at p. 801.)[6]

The Court expressed concern that auto buyers might not learn of the sales tax reimbursement refund process, as retailers were not required to notify their customers. (*Javor*, *supra*, 12 Cal.3d at p. 801.) The Court also noted that even though "[t]he Board has admitted that it must pay these refunds to retailers[,]" because "the retailer cannot retain the refund himself, but must pay it over to his customer, the retailer has no particular

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[6] Amicus Bekkerman misstates the facts of *Javor*. (Bekkerman 40.) In that case, there was no suggestion that the agency returned sales tax refunds to retailers without conditioning the return on the retailers' making corresponding refunds of sales tax reimbursement to consumers. Indeed, 12 years before, in *Decorative Carpets, supra,* 58 Cal.2d 252, the Court had approved the Board's practice of conditioning refunds to retailers on the retailers' returning the reimbursement to paying customers.

incentive to request the refund on his own." (*Id.* at pp. 801, 802.) And it observed that "[t]he integrity of the sales tax requires not only that the retailers not be unjustly enriched ..., but also that the state not be similarly unjustly enriched." (*Id.* at p. 802.)

The *Javor* Court held that in these "unique circumstances," the class of consumers who had paid sales tax reimbursement calculated on the pre-adjustment sales price were entitled to sue to "compel defendant retailers to make refund applications to the Board" and for the Board to take the "minimal action" of "pay[ing] the refund owed the retailers into court or provid[ing] proof to the court that the retailer had already claimed and received a refund from the Board." (*Javor*, *supra*, 12 Cal.3d at p. 802.)

The considerations underlying recognition of a special consumer remedy in *Javor* do not justify the judicial creation of a more general, consumer-initiated cause of action seeking the return of sales tax reimbursement on the theory that retailers could have claimed sales tax exemptions, but did not do so. There is not, for example, the same type of incentive problem present in *Javor*, which involved a post-sale retroactive sales tax adjustment. In that case, while there were sales tax refunds simply waiting for the auto dealers to claim them and to pass corresponding sales tax reimbursement back to auto buyers, there was no ongoing relationship between the dealers and the affected buyers. In that case, there was little incentive for retailers to search out buyers in completed transactions who had already taken delivery of their vehicles and departed. In contrast, retailers generally have an incentive in every prospective transaction to claim sales tax exemptions so that they may attract consumers by offering goods at a lower total cost and gain a market advantage. (See ABM 39 & fn. 19.) Nor do sales tax exemptions present the type of unintended windfall at issue in *Javor*. By statute, all retail sales are presumptively taxable, and sales tax exemptions may be waived. (See ABM 37-38.)

Accordingly, the State's receipt of tax on a sale as to which an exemption arguably could have applied is not unjust, but rather the natural result of a legislative design that presumes taxability and allows exemptions to be waived. And there can of course be no unjust enrichment to the retailer in these circumstances, provided all sales tax reimbursement collected is reflected in the retailer's remittance to the State—as the law requires.

Most importantly, the agency in *Javor* had already determined that sales tax refunds to retailers, and the retailers' return of corresponding sales tax reimbursement to customers, were appropriate for a defined set of transactions based on a post-sale change in the law, and no question of taxability was left to decide. That is not true in this case. Whether a sales tax exemption could apply in any given transaction is often a complex, fact-intensive inquiry. (*Loeffler, supra,* 58 Cal.4th at pp. 1103, 1105-1106 [citing examples], 1127; ABM 21-24, 37 [citing examples]; see also Cal. Code Regs., tit. 18, § 1603, subd. (c)(2)(B) [determination of taxability of sales of cold food "to go" is determined on a location-by-location basis].) Here, plaintiffs seek a determination of whether the conditional sales tax exemption for the sale of glucose test strips and lancets could apply in a variety of complex and diverse factual circumstances—sold off the shelves or rather from a controlled space; by a licensed pharmacy or a registered pharmacist; with or without written proof of being under a doctor's care. (ABM 24-25, 37.) The potential taxability of the sale of these items in these various scenarios "was 'very hotly in dispute.'" (*McClain v. Sav-on Drugs* (2017) 9 Cal.App.5th 684, 691 [quoting the trial court].) As this Court held in *Loeffler*, disputes about whether an exemption might apply to a specific transaction cannot be resolved in the first instance by a court, because "[t]he Legislature has subjected such questions to an administrative exhaustion requirement precisely to obtain the benefit of the Board's expertise, permit it to correct mistakes, and save judicial resources."

(*Loeffler*, *supra*, 58 Cal.4th at p. 1127; see generally § 6932; ABM 19-20.) By statute, the vehicle for exhaustion is a taxpayer-initiated administrative claim for refund. (*Ibid.*)

C. Referral to the Department of Taxability Questions Raised in Consumer-Initiated Refund Lawsuits Would Be Inconsistent with the Tax Code and Unworkable as a Practical Matter

Amici suggest that to address the above concerns, a court might refer consumers' contentions about the application of sales tax exemptions to the Department for decision in the first instance. (Consumer Attorneys 18 [discussing primary jurisdiction doctrine and suggesting referral of taxability question to Department]; Littlejohn 6-7 [suggesting that consumer-initiated court action should trigger administrative proceeding on taxability]; Public Citizen 9-10 [similar]; see also RBM 16-17, 30 [similar]; *Loeffler*, *supra*, 58 Cal.4th at p. 1140 (dis. opn. of Liu, J.) [proposing joinder of Board in litigation of consumer UCL claims challenging sales tax reimbursement].) This approach is flawed for at least three reasons.

First, the Legislature has not charged the Department with resolving *consumers*' disagreements with taxpaying *retailers*' routine business decisions not to assert sales tax exemptions as to specific transactions. As this Court noted in *Loeffler*:

> The tax code does not permit consumers to *require* the Board to ascertain whether excess reimbursement charges have been made. Rather, with respect to excess reimbursement charges, section 6901.5 contemplates that it is for the Board to ascertain under its normal procedures whether any mistake has been made. If the matter is not raised through an audit or a deficiency determination, it is for the taxpayer to claim a refund from the Board, which may in turn require the taxpayer to refund excess reimbursement to consumers.

(*Loeffler*, *supra*, 58 Cal.4th at p. 1128, original italics;[7] see also State Bd. of Equalization, operations memo No. 611 (Oct. 23, 1978) p. 4 [observing that after the 1978 amendment repealing former section 6054.5, the agency has "no statutory duty to police the retail trade to ensure that only the correct amount of tax reimbursement is collected from the customers on retail sales"], cited in *Loeffler*, *supra*, 58 Cal.4th at p. 1117; State Bd. of Equalization, operations memo No. 754 (Jan. 12, 1983) pp. 1-3 [explaining that under section 6901.5, a taxpayer/retailer has not collected excess sales tax reimbursement from a consumer where the amount collected does not exceed the amount of the retailer's own tax-related liabilities on the same transaction—in the form of sales or use tax owed to the State, or sales or use tax reimbursement owed to another], discussed generally in *Loeffler*, *supra*, 58 Cal.4th at p. 1119.)[8] "[U]nder the Board's annotations, the consumer lacks standing in disputes over the application of the tax law to particular transactions." (*Loeffler*, *supra*, 58 Cal.4th at p. 1128, citing State Bd. of Equalization, Business Taxes Law Guide, Sales & Use Tax Annots.,

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[7] To be clear, the "normal procedures" for ascertaining any such excess are those established by statute—specifically, in the main, audits, deficiency determinations, and refund proceedings. (See *Loeffler*, *supra*, 58 Cal.4th at p. 1120.)

[8] Howard Jarvis argues that the tax code, by failing to provide for any cause of action by consumers to seek refunds related to sales tax exemptions, "is in irreconcilable conflict with Civil Code section 3523," an 1872 maxim of jurisprudence that "promises that '[f]or every wrong there is a remedy.'" (Howard Jarvis 10, 22-23.) Amicus misunderstands the function of the maxims. While maxims may assist a court in exercising its equitable powers or in construing statutes, they cannot be employed to override legislative intent (*National Shooting Sports Foundation, Inc. v. State of California* (June 28, 2018, S239397) __ Cal.5th __ [2018 WL 3150950, *2], or create remedies not intended by the Legislature (see *Tulare County v. Kings County* (1897) 117 Cal. 195, 202-203 (per curiam)).

Annot. No. 460.0028 ["There is no provision in the law for an action on the part of a nontaxpayer to dispute the application of tax."].)[9]

There is, therefore, no established "'pervasive and self-contained system of administrative procedure'" ready to accept court-referred questions presented in consumer-initiated actions. (Compare *Farmers Ins. Exchange v. Superior Court* (1992) 2 Cal.4th 377, 396.) And requiring the Department to hear and resolve such consumer-initiated disputes on court referral could substantially interfere with the Department's ability to carry out its statutory responsibilities, which likely would be displaced by "a huge volume of litigation over all the fine points of tax law as applied to millions of daily commercial transactions in this state" taking place "outside the system set up by the Legislature[.]" (See *Loeffler*, *supra*, 58 Cal.4th at p. 1130 [declining to recognize similar claims under the Unfair Competition Law and Consumer Legal Remedies Act based in part on the potential effect on the courts]; see also *id.* at p. 1103 ["whether a particular sale is subject to or is exempt from sales tax, is exceedingly closely regulated, complex, and highly technical"]; ABM 36-37; cf. RBM 27 [suggesting that the Department should review the taxability of all sales of glucose test strips and lancets by defendant retailers in California since 2000].)[10]

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[9] All annotations bearing on sales tax reimbursement are available at <http://www.boe.ca.gov/lawguides/business/current/btlg/vol2/suta/460-0000.html> [as of July 10, 2018].

[10] Resolving the referral would likely involve a number of steps and could cause significant delay to the court proceedings. To take one example, sales taxes are calculated based on gross receipts received during the taxable period (§ 6051) and, therefore, retailers' reporting to the Department is not segregated by type of sale. In order to determine whether retailers paid tax on particular types of sales at issue in the referral, the Department would need to audit each relevant retailer. As a result, the

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Second, the referral approach fails to recognize that all covered retail sales are presumptively taxable (*Loeffler*, *supra*, 58 Cal.4th at p. 1107; § 6091); the retailer bears both the burden of establishing any exemption (*id.* at p. 1107; § 6091) and the administrative costs of doing so (see *Paine v. State Bd. of Equalization* (1982) 137 Cal.App.3d 438, 443); and the retailer reasonably may decline to assert sales tax exemptions, even where they apply—or might arguably apply (§§ 6901.5, 6905, 6933). (See *Loeffler*, *supra*, 58 Cal.4th at p. 1105 [discussing exemptions and noting "complicated and fact-specific exemptions for some sales of food or medicine"]); *id.* at p. 1129 [noting that in light of these circumstances, "it would not be unreasonable if the retailer's tax payment to some extent erred on the side of considering sales taxable"]; see also *id.* at p. 1141 (dis. opn. of Liu, J.) [similar].)[11]

Finally, referral to the Department does nothing to address the uncertainty caused by a multiplicity of large-scale consumer class actions challenging taxpayer-retailers' decisions about whether to claim sales tax exemptions on completed transactions that are otherwise settled as between retailers and the Department. (ABM 38.) With or without referral, recognizing such claims could severely undermine the predictability of the State's sales tax revenues and contravene the purposes of Section 32, which include "'avoid[ing] unnecessary disruption of public services'" dependent

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court case would likely have to be stayed until the audits, and any appeals taxpaying retailers might pursue (including litigation), were final and non-appealable.

[11] Amici imply without citation that it is "illegal" for a retailer to collect sales tax reimbursement on a transaction that could in theory be claimed as tax exempt. (Consumer Attorneys 12; see also Bekkerman 36, 40, 43.) In fact, as section 6901.5 provides, there is nothing illegal in such a practice—provided the retailer remits the amount to the State.

on tax revenues and allowing "'governmental entities [to] engage in fiscal planning based on expected tax revenues.'" (See *Loeffler*, *supra*, 58 Cal.4th at pp. 1101, 1102, 1131, quoting *Woosley v. State of California* (1992) 3 Cal.4th 758, 789.)

D. *Javor* Must Be Limited to Circumstances Where the Department Has Already Determined, Pursuant to Normal Statutory Procedures, That a Sales Tax Refund Is Due

For these reasons, *Javor* claims should be limited to situations where, at the time of filing, the Department or the Legislature has already defined or recognized a set of sales transactions that require a sales tax refund, and the Department has already completed any necessary interpretation of law and application of fact to law such that "[t]here [is] no controversy over the taxability question" and there can be no dispute that "an excess had been collected" and "the amount of the excess also [is] not in dispute." (See *Loeffler*, *supra*, 58 Cal.4th at p. 1115, fn. 10 [summarizing *Javor*]; ABM 34, fn. 15.)[12] Issues of taxability must be sufficiently settled such that on receipt of the retailers' court-compelled refund requests, the only thing the Department needs to do is to check each request for refund against the established criteria, and calculate or confirm the refund due using basic math. This rule makes the *Javor* remedy a limited one, but one that follows from *Javor* itself, which recognized that the remedy would not be common. (*Javor*, *supra*, 12 Cal.3d at p. 802 [allowing for equitable remedy "under

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[12] Amicus Consumer Attorneys asserts that without broad *Javor* relief, there is "no meaningful incentive to businesses" to assert sales exemptions (and therefore refrain from collecting sales tax reimbursement). (Consumer Attorneys 5; see also *id.* at 7.) The Department disagrees. In general, there is a market incentive for retailers to offer goods at a lower total cost (ABM 39), and retailers routinely claim sales tax exemptions—as a review of any typical set of household receipts will confirm.

the unique circumstances of this case"].) To maintain that limited scope, no *Javor* claim may lie where the consumer-plaintiff's only allegation is that a retailer could have asserted a sales tax exemption, but did not do so.

Contrary to amici's suggestions, limiting *Javor* relief to situations where the Department has already settled any open issues of taxability and has concluded that sales tax refunds are due to retailers in a set of identified transactions (and therefore that sales tax reimbursement must in turn be refunded to consumers) would not sanction or encourage the Department to obstruct valid, *Javor*-type reimbursement refund actions simply by failing to take action. (See Bekkerman 39, 41; Howard Jarvis 12; Littlejohn 1, 4, 9; Public Citizen 10-11; RBM 34-35, 37.) As this Court has observed, the Department "has a vital interest in the integrity" of the sales tax system. (*Decorative Carpets*, *supra*, 58 Cal.2d at p. 255.) In the unusual circumstances presented in *Javor*, this interest motivated the Department to determine that sales tax refunds were due—even though many retailer/taxpayers did not request refunds (because the retailers would not benefit from refunds, but would be required to pass the amounts back to buyers who had paid sales tax reimbursement). And, to the extent the Legislature decides that the Department should make sales tax refund determinations for the benefit of non-taxpayers (consumers), it can by statute direct the Department to take action. (See, e.g., § 7277 [where local sales tax determined to be unconstitutional, establishing procedure for consumers to seek return of sales tax reimbursement from State impound account]; § 7279.6 [providing that "[a]n arbitrary and capricious action of the board in implementing the provisions of this chapter shall be reviewable by writ"]; see also *Kuykendall v. State Bd. of Equalization* (1994) 22 Cal.App.4th 1194, 1211-1215, discussed at ABM 20, fn. 8, 48.) Once the agency has taken the action required by the Legislature, and if the other

conditions noted above are satisfied, a *Javor* claim—if necessary—could follow.

II. DECLINING TO EXTEND *JAVOR* TO THE CIRCUMSTANCES OF THIS CASE DOES NOT VIOLATE DUE PROCESS

As this Court recently confirmed, it is the Legislature's prerogative to decide that sales tax is imposed on retailers for the privilege of selling tangible personal property, and not on consumers, notwithstanding that consumers commonly reimburse sellers for sales tax as a matter of contract. (See *Loeffler*, *supra*, 58 Cal.4th at pp. 1104, 1127-1129.)

A. While Consumers Benefit Indirectly from Sales Tax Exemptions, Such Indirect Interests Are Not Protected by Due Process

Amici Bekkerman and Howard Jarvis reassert plaintiffs' argument that unless a refund remedy is extended to consumers on the facts of this case, California's sales tax system violates consumers' right to due process. (Bekkerman 16-29, 32-45; Howard Jarvis 16-18, 20-23; see also RBM 4-13.) Amici's constitutional arguments presume that consumers are the true taxpayers because, amici assert, they bear the ultimate economic burden of retail sales taxes. Amici's due process arguments fail for the reasons stated in the Department's answer brief—chief among them being that consumers, by statutory design, are not the taxpayers; they are burdened by sales taxes, and benefit from sales tax exemptions, only indirectly. (ABM 17-18, 43-50.) The Due Process Clause "does not apply to the indirect adverse effects of governmental action." (*O'Bannon v. Town Court Nursing Center* (1980) 447 U.S. 773, 789; cf., *South Carolina v. Regan* (1984) 465 U.S. 367, 394, fn. 11 (concur. opn. of O'Connor, J.) [though taxes "inevitably have a pecuniary impact on nontaxpayers[,]" the "indirect impacts of a tax, no matter how detrimental, generally do not invade any interest cognizable under the Due Process Clause"].) (ABM 49.)

B. Federal Cases Addressing Federal Tax Immunity Are Inapposite

Contrary to amici's arguments, federal decisions concerning the legal incidence of sales taxes for purposes of *federal immunity*, including the U.S. Supreme Court's decision in *Diamond National Corp. v. State Board of Equalization* (1976) 425 U.S. 268 (per curiam), do not require this Court to disregard the Legislature's decision to designate retailers, and not consumers, as taxpayers. (See Bekkerman 16-29; Howard Jarvis 12, 14-16; ABM 47-48 & fn. 29.)[13]

In *Diamond National*, the Court held that for purposes of federal immunity, the incidence of California's sales tax (as state tax law was then structured) fell on a national bank as the purchaser of forms and other tangible personal property, rather than on the vendor; under federal law, the bank was therefore exempt from state taxes. (425 U.S. 268.) A decision does not, of course, stand for propositions not considered by the court. (*Loeffler*, *supra*, 58 Cal.4th at p. 1134.) *Diamond National*'s holding with respect to federal tax immunity thus does not establish that California consumers are retail sales taxpayers for the more general purposes of due process.

Where an interest asserted to be protected by due process is grounded in state law, courts look to the provisions of that law to determine whether

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[13] The many additional cases cited by amicus Bekkerman that involve federal and tribal tax immunity—not due process—are thus of little assistance. (See *Kern-Limerick, Inc. v. Scurlock* (1954) 347 U.S. 110; *First Agricultural Nat. Bank v. State Tax Com.* (1968) 392 U.S. 339; *U.S. v. State Tax Com. of Miss.* (1975) 421 U.S. 599; *Cal. State Bd. of Equalization v. Chemehuevi Indian Tribe* (1985) 474 U.S. 9 (per curiam); *U.S. v. Nevada Tax Com.* (9th Cir. 1971) 439 F.2d 435; *U.S. v. New Mexico* (10th Cir. 1978) 581 F.2d 803; *U.S. v. Cal. State Bd. of Equalization* (9th Cir. 1981) 650 F.2d 1127, affd. (1982) 456 U.S. 901; and *Coeur D'Alene Tribe v. Hammond* (9th Cir. 2004) 384 F.3d 674.)

the interest amounts to a constitutionally protected liberty or property right, as opposed to a mere desire or "unilateral expectation." (*Town of Castle Rock v. Gonzales* (2005) 545 U.S. 748, 757, quotation omitted; see also *Gurley v. Rhoden* (1975) 421 U.S. 200, 203, 208 [rejecting gasoline distributor's due process claim premised on theory that legal incidence of state excise tax was on consumer; holding state court's interpretation of its tax law placing legal incidence on distributor "conclusive" because interpretation was "consistent with the statute's reasonable interpretation"]; see ABM 49-50.) As noted, by its terms, California sales tax law affects consumers only indirectly, expressly designating retailers and not consumers as taxpayers, and, therefore, consistent with state and federal due process requirements, does not provide consumers with tax refund remedies.

In addition, *Diamond National* does not reflect the current state of California sales tax law. As summarized in *Loeffler*, the Legislature responded to *Diamond National* "'by *removing* from the code those provisions of law which have characteristics of laws which impose the *tax upon the consumer*.'" (58 Cal.4th at p. 1116, quoting Assem. Com. on Revenue & Taxation, Analysis of Sen. Bill No. 472 (1977-1978 Reg. Sess.) as amended June 15, 1977, p. 3 [italics in *Loeffler*].) Provisions removed include former sections 6052 and 6053, which contained language suggesting that the retailer was required to collect reimbursement. (*Loeffler*, *supra*, 58 Cal.4th at pp. 1116-1117.) And the Legislature added language to Civil Code section 1656.1 clarifying that retailers could, but were not required to, seek reimbursement for sales tax from consumers by contract. (*Id.* at p. 1117.)[14]

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[14] Shortly after these amendments, the Ninth Circuit held for purposes of federal tax immunity that the legal incidence of state sales tax (continued...)

C. Consumers Are Not Effectively Forced to Pay Sales Tax; They Engage in Voluntary Transactions Governed by Contract Law

Howard Jarvis further contends that consumers effectively are forced to pay sales tax but have no meaningful opportunity for a hearing or review. (Howard Jarvis 8-9, 12, 13-14, 18; see also RBM 3.) That argument misunderstands the case on which it relies, *National Ice and Cold Storage Co. of California v. Pacific Fruit Express Co.* (1938) 11 Cal.2d 283. (See Howard Jarvis at 8-9, 13, 15-16, 18, 19, 21.)

In *National Ice*, the Court examined the initial iteration of the Retail Sales Act, which became effective in 1933. (*National Ice*, *supra*, 11 Cal.2d at p. 285.) The law imposed a tax on retailers for the privilege of selling tangible personal property, but also provided that retailers had a right to add sales tax to the sales price and to collect it from the buyer. (*Id.* at pp. 285-286.) Seven years before the law took effect, plaintiff, an ice purveyor, had entered into a written contract with defendant, an express shipping company, to provide ice for the refrigeration of rail cars. (*Id.* at pp. 286-287.) "At no time did the agreement contain any provision relative to the payment by either party of any sales tax such as was contemplated by the

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(...continued)
associated with equipment leasing remained on the United States as lessee. (*U.S. v. Cal. State Bd. of Equalization* (1981) 650 F.2d 1127, affd. without opinion (1982) 456 U.S. 901.) (See Bekkerman 23-26; ABM 47-48, fn. 29.) Again, that decision is not helpful in analyzing a due process claim. Moreover, even as to federal tax immunity, the decision appears to be in tension with more recent U.S. Supreme Court decisions involving tribal tax immunity that rely on state legislatures' use of "dispositive language" concerning the legal incidence of a state tax and the "'fair interpretation'" of the state taxing statute as written and applied. (*Wagnon v. Prairie Band Potawatomi Nation* (2005) 546 U.S. 95, 102-103, quoting *Cal. Bd. of Equalization v. Chemehuevi Tribe, supra,* 474 U.S. at p. 11; see ABM 47-48, fn. 29.)

provisions of the 'Retail Sales Tax Act of 1933,' or otherwise." (*Id.* at p. 286.) After the Act took effect, the ice company demanded that the express company pay "an additional sum of money, equal to the amount of the tax which had accrued on the gross amount of the purchase price" of the delivered ice, which the express company refused to pay. (*Id.* at p. 287.) The seller then brought suit. (*Ibid.*)

The Court rejected the seller's argument that—notwithstanding the Act's statement that the tax was "imposed upon retailers" (*National Ice, supra*, 11 Cal.2d at p. 285)—the Legislature's intent was "that in reality the consumer should pay the tax." (*Id.* at p. 288.) "[I]t would have been within the power of the Legislature to have imposed a tax upon either the retailer or the purchaser of such property[.]" (*Id.* at p. 290.) As the Court observed, the Legislature's express choice was to impose the tax "upon the retailer, and not upon the consumer[.]" (*Id.* at p. 289.)

The Court struck down the provision of the Act that purported to create by statute "a legal right of the retailer to 'pass on' to the consumer a tax which by the terms of the statute has been imposed directly on the retailer[.]" (*National Ice, supra,* 11 Cal.2d at pp. 290, 291.) "[T]o baldly legislate that without, and in the absence of either due or any process of law, a legal debt that is owed by one person must be paid by another, is quite at variance with ordinary notions of that which may be termed the administration of justice." (*Id.* at p. 291.) Still, the Court noted that its ruling was "not intended to indicate the illegality of authority which may be lodged in a retailer to 'pass on' the tax to a purchaser with the latter's *consent* thereto, either expressly or impliedly given. That sort of arrangement between interested parties in such a sale is not here involved." (*Id.* at p. 292, italics added; see also *De Aryan v. Akers* (1939) 12 Cal.2d 781, 786 [confirming that *National Ice* did not preclude reimbursement by contract].)

D. Contractual "Consent" Does Not Mean That Consumers Must Be Given an Opportunity to Dispute the Routine Application of Sales Tax Exemptions

Contrary to amici's assertions (see Bekkerman 30-31, 36-37; Howard Jarvis 17-18), "consent" in the context of *National Ice* does not mean that in every retail sale, the consumer, a non-taxpayer, must be given an opportunity to dispute issues of sales tax law that may touch the transaction—for example, that a sales tax is due, or that a sales tax exemption does not apply or will not be pursued. (See *De Aryan, supra,* 12 Cal.2d at pp. 783, 785 [rejecting claim by buyer against seller that one-cent sales tax reimbursement added to 15-cent sales price was and "exaction" and excessive].)[15] Rather, "consent' means that the consumer must contractually agree to the tax-related payment term. The seller's offer for sale may include an additional sum to be paid as sales tax reimbursement—a term that the consumer may either accept (by paying the sums requested and taking away the item on offer), or reject. When the seller's offer includes sales tax reimbursement, "[t]he consumer still has the right to purchase or not at the asked price which includes the tax." (*Id.* at p. 786.)[16]

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[15] The *De Aryan* Court took the matter "because of what was deemed to have been a mistaken application of certain language appearing in our [*National Ice*] decision ...." (12 Cal.2d at p. 783.)

[16] A consumer may also simply refuse to pay sales tax reimbursement—even if required by contract—in which case the retailer will still owe taxes. (See State Bd. of Equalization, Business Taxes Law Guide, Sales & Use Tax Annots., Annot. No. 460.0180 [purchaser DMV's refusal to pay sales tax on paper sold to it does not exempt paper retailer's tax liability].) Accordingly, and contrary to the argument of Howard Jarvis, a consumer is never "forced to pay the 'retailer's' tax obligations[.]" (See Howard Jarvis 18.) Neither does a contractual agreement to pay sales tax reimbursement amount to "extortion." (See Bekkerman 37-38, quotation omitted.)

This understanding of the rule of *National Ice* is reflected in Civil Code section 1656.1. The provision expressly provides that "[w]hether a retailer may add sales tax reimbursement to the sales price of the tangible personal property sold at retail to a purchaser depends solely upon the terms of the agreement of sale[,]" and sets out conditions allowing for a rebuttable presumption that the parties agreed to include this term—for example, where "[s]ales tax reimbursement is shown on the sales check or other proof of sale[.]" (Civ. Code, § 1656.1, subds. (a), (b), (d).)

Howard Jarvis further asserts that consumers "no longer have an effective opportunity to rebut the presumption" as provided by subdivision (d). (Howard Jarvis 11-12; see also RBM 1.) This argument ignores the primary function of subdivision (d): It preserves the *Department's* ability to rebut a retailer's assertion that the retailer's gross receipts (the amount on which sales tax is calculated (§ 6012)) exclude sales tax reimbursement charges. (See ABM 17.) The argument is also incorrect. Normal rules of contract interpretation apply as between the retailer and the consumer. If, for example, a contract for sale included a pre-printed statement that sales tax reimbursement would be added, but a handwritten addition to the contract stated that the seller would "pay the sales tax," the consumer could make the case that the handwritten term should control. (See Civ. Code, § 1651).[17]

CONCLUSION

The Department acknowledges the economic burdens facing thousands of Californians who are living with diabetes. Over the years, the Department has taken a variety of actions within the limits of its statutory

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[17] Bekkerman also makes passing reference to takings jurisprudence (Bekkerman 37-38), but the property-development cases cited are not factually or legally similar to this case. (See ABM 50, fn. 50.)

authority to encourage retailers to claim sales tax exemptions for glucose test strips and lancets—even as the Legislature considered but declined to enact a statutory exemption. (ABM 22-23.) The Department's actions include promulgating a regulation expanding the statutory exemption for prescription medicines to reach these products (over objections that the regulation was overbroad); conducting a statewide survey of retailers to understand whether and how its regulation was being implemented; issuing a letter to 13,000 retailers clarifying that a formal prescription was not required for these products; and issuing various plain-language guidance documents providing informal guidance on the regulatory exemption. (ABM 21-24.) Arguments that more could be done to encourage retailers to claim sales tax exemptions for these products speak to matters of policy, and may always be addressed either to the Department or to the Legislature. They do not justify the creation of novel, unwieldy, and burdensome litigation-based remedies by the courts.

The trial court did not err in sustaining defendants' demurrer to plaintiff consumers' complaint without leave to amend. The Court of Appeal's judgment upholding that decision should be affirmed.

Dated: July, 12 2018

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CERTIFICATE OF COMPLIANCE

I certify that the attached Respondent California Department of Tax and Fee Administration's Consolidated Answer to Amicus Curiae Briefs uses a 13 point Times New Roman font and contains 6,886 words.

Dated: July 12, 2018

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DECLARATION OF SERVICE BY U.S. MAIL

Case Name: **Michael McClain v. Sav-On Drugs, et al.**
Case No.: **S241471**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar, at which member's direction this service is made. I am 18 years of age or older and not a party to this matter. I am familiar with the business practice at the Office of the Attorney General for collection and processing of correspondence for mailing with the United States Postal Service. In accordance with that practice, correspondence placed in the internal mail collection system at the Office of the Attorney General is deposited with the United States Postal Service with postage thereon fully prepaid that same day in the ordinary course of business.

On July 12, 2018, I served the attached **RESPONDENT CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION'S CONSOLIDATED ANSWER TO AMICUS CURIAE BRIEFS** by placing a true copy thereof enclosed in a sealed envelope in the internal mail collection system at the Office of the Attorney General at 455 Golden Gate Avenue, Suite 11000, San Francisco, CA 94102-7004, addressed as follows:

[See attached service list]

I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on July 12, 2018, at San Francisco, California.

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Declarant

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