
THIRD READING

Bill No: SB 1406
Author: McNerney (D), et al.
Amended: 4/23/26
Vote: 27- Urgency

SENATE REVENUE AND TAXATION COMMITTEE: 4-0, 5/6/26
AYES: McNerney, Ashby, Becker, Grayson
NO VOTE RECORDED: Alvarado-Gil

SENATE APPROPRIATIONS COMMITTEE: Senate Rule 28.8

SUBJECT: Sales and Use Tax Law: vehicles: shell companies

SOURCE: Author

DIGEST: This bill allows the California Department of Tax and Fee Administration (CDTFA) to hold personally liable any officer, manager, partner, beneficial owner, or member of a shell company for any unpaid taxes on the purchase of a vehicle, vessel, or aircraft.

ANALYSIS:

Existing law:

- 1) Imposes the sales tax on every retailer “engaged in business in this state” that sells tangible personal property and requires them to register with the CDTFA, as well as remit taxes collected from purchasers to CDTFA.
- 2) Applies the sales tax whenever a retail sale occurs, which is generally any sale other than one for resale in the regular course of business.
- 3) Provides that unless the purchaser pays the sales tax to the retailer, they are liable for the use tax, which is imposed on any person consuming tangible personal property in the state, and requires the purchaser to remit use tax to CDTFA.

- 4) Sets the state sales and use tax rate at 7.25% of the sales price of the property sold or used, of which 3.9375% flows to the state General Fund.
- 5) Imposes use tax on all original registration and transfer applications for vehicles and vessels purchased from someone other than a licensed California dealer, manufacturer, or dismantler.
- 6) Does not impose sales or use tax when a California resident purchases a vehicle for use outside of California.
- 7) Establishes a rebuttable presumption that when a vehicle is purchased outside of California, is first functionally used outside of California, and is brought into California within 12 months from the date of its purchase, the vehicle was purchased for use in California and is subject to use tax if any of the following occur:
 - a) The vehicle is purchased by a California resident.
 - b) The vehicle is subject to California Department of Motor Vehicles (DMV) registration during the first 12 months of ownership.
 - c) If purchased by a nonresident of California, the vehicle is used or stored in California more than one-half of the time during the first 12 months of ownership.
- 8) Authorizes CDTFA to impose and collect taxes for the vehicles purchased by a closely held corporation or limited liability company out of state and subsequently brought into California within the first 12 months of ownership, from the company but not its member owners.

This bill:

- 1) Allows CDTFA to hold personally liable any officer, manager, partner, beneficial owner, or member of a shell company for any unpaid taxes on the purchase of a vehicle, vessel, or aircraft.
- 2) Defines “shell company” as a closely held corporation, partnership, limited partnership, limited liability partnership, or limited liability company used for the purpose of evading the payment of taxes due under this part.
- 3) Evidence that an entity is a shell company used for the purpose of evading the tax includes, but is not limited to, any of the following:

- a) It lacks a specific business activity or purpose.
 - b) It fails to maintain a physical location outside California.
 - c) It fails to employ individual persons and provide those persons with Internal Revenue Service Form W-2 wage and tax statements.
 - d) It fails to file federal tax returns or fails to file a required state tax return in a state other than California.
- 4) Expands the list of business types that are considered California “residents” when 50% of the business memberships’ interests are held by a California resident to include partnerships, limited partnerships, and limited liability partnerships.
 - 5) Specifies that a shell company shall be deemed to be a California “resident” if any shareholder, partner, member, or beneficial owner is a resident of California.
 - 6) Makes other technical amendments.

Background

The “Montana LLC Loophole”. According to CDTFA, California loses approximately \$20 million in use tax revenue each year from the purchase of luxury vehicles, yachts, RVs, and aircraft due to a fraudulent tax scheme involving limited liability companies (LLCs) domiciled in Montana. To evade sales and use tax on their purchases, some California residents form a shell company LLC domiciled in Montana and buy the vehicle in the Montana LLC’s name, where they then take delivery of the vehicle outside the state and register the vehicle in Montana, where no sales or use tax applies, and subsequently return the vehicle to California within 12 months of purchase. Some California dealers may be complicit in this tax avoidance strategy, as they can lower the transaction cost and relieve themselves of any related sales tax liability by delivering the vehicle to the purchaser outside the state.

Department of Justice enforcement actions. On March 6, 2026, the California Attorney General, together with the DMV and CDTFA, announced charges against 14 individuals for their alleged roles in a scheme to evade the reporting of over \$20 million in luxury vehicle purchases to avoid paying over \$1.8 million in California taxes. The vehicles included a \$1.8 million McLaren Elva, a \$1.5 million Porsche 918 Spyder, and a \$1.26 million Ferrari F12TDF, among others. The individuals were charged in a 56-count complaint for criminal sales tax evasion, including

conspiracy, filing false sales tax returns, failing to file tax returns, perjury, and money laundering. These charges were filed after a 2024 investigation by DMV, CDTFA, and the California Department of Justice revealed a scheme stretching back to 2018.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: Yes

SUPPORT: (Verified 5/12/26)

California Teachers Association
SEIU California

OPPOSITION: (Verified 5/12/26)

None received

ARGUMENTS IN SUPPORT: According to the author, “California loses approximately \$20 million in tax revenues a year due to the so-called ‘Montana Loophole,’ which enables California tax evaders to form out-of-state shell companies to purchase and register vehicles tax-free to avoid paying California taxes. SB 1406 would strengthen California law by making it easier to collect taxes from tax evaders that create an out-of-state shell companies to buy exotic luxury cars or expensive recreational vehicles in Montana or other states.”

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**** END ****