

[Assembly Bill 479](#) (Gonzalez-Fletcher & C. Garcia)

Date: 03/27/17

Program: Sales and Use Tax

Sponsor: Authors

Revenue and Taxation Code Sections 6369.8, 32220, & 32221.5

Effective: Upon enactment, but operative January 1, 2018

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Summary: Exempts feminine hygiene products and diapers from the sales and use tax while increasing the distilled spirits surtax by \$1.20 for 100 proof and under, and \$2.40 for over 100 proof.

Purpose: According to the author, to eliminate sales and use tax on three essential health supplies for women and children.

Fiscal Impact Summary: Annual net revenue loss of \$59 million (diaper and feminine hygiene sales tax exemptions of \$139 million, offset by distilled spirits surtax gain of \$80 million).

Existing Law: Except where the law provides a specific exemption or exclusion, California's Sales and Use Tax Law¹ imposes the sales tax on all retailers for the privilege of selling tangible personal property at retail in this state or the use tax on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer.

Existing law provides numerous exemptions from the sales and use tax. Some of the more significant exemptions relate to "necessities of life," including:

- Food, as specified and defined.²
- Prescription medicines, as specified and defined.³
- Gas, electricity, and water sold to consumers through mains, lines, and pipes.⁴
- "Food" animals, such as cows, pigs and chickens, and "food" plants, such as asparagus, nut trees, and strawberry plants.⁵

The sales and use tax is imposed on a variety of other "necessities of life" sold at retail, such as feminine hygiene products, toilet paper, clothing, shoes, soap, and baby and adult diapers and other incontinence products.

California's sales and use tax rates. As of January 1, 2017, California's statewide sales and use tax rate is 7.25%. The table below shows California's various sales and use tax rate components (the table excludes voter-approved city and county district taxes):

Rate	Jurisdiction	Purpose/Authority
3.9375%	State (General Fund)	State general purposes (RTC Sections 6051, 6051.3, 6201, 6201.3)
0.50%	State (Local Public Safety Fund)	Local governments to fund public safety services (Section 35, Article XIII, State Constitution)
0.50%	State (Local Revenue Fund)	Local governments to fund health and welfare programs (RTC Sections 6051.2 and 6201.2)
1.0625%	Local Revenue Fund 2011	Realignment of local public safety services (RTC Sections 6051.15 and 6201.15)

¹ Part 1 of Division 2 of the Revenue and Taxation Code (RTC) (commencing with Section 6001).

² RTC Section 6359.

³ RTC Section 6369.

⁴ RTC Section 6353.

⁵ RTC Section 6358.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the BOE's formal position.

Rate	Jurisdiction	Purpose/Authority
1.25%	Local (City/County) 1.00% City and County 0.25% County	(RTC Sections 7202 and 7203) General city and county operations County transportation purposes
7.25%	Total Statewide Rate	

Alcoholic Beverage Tax Law: Under existing law,⁶ the following taxes and surcharges are imposed on the sale of beer, wine, and distilled spirits:

Product	Per Gallon Tax	Per Gallon Surcharge	Total per Gallon
Beer	\$0.04	\$0.16	\$0.20
Wine (not more than 14 percent alcohol)	\$0.01	\$0.19	\$0.20
Wine (more than 14 percent alcohol)	\$0.02	\$0.18	\$0.20
Sparkling wine	\$0.30	\$0.00	\$0.30
Hard cider	\$0.02	\$0.18	\$0.20
Distilled spirits (100 proof)	\$2.00	\$1.30	\$3.30
Distilled spirits (100+ proof)	\$4.00	\$2.60	\$6.60

The taxes and surcharges collected are deposited into the Alcohol Beverage Control Fund and withdrawn for use by the State’s General Fund or used to pay refunds.

The surtax on beer, wine, and distilled spirits was last changed in 1991 by Assembly Bill 30 (Ch. 86, Stats. 1991).

Proposed Law: Beginning January 1, 2018, this bill exempts from the sales and use tax sales and purchases of:

- Wearable incontinence supplies designed, manufactured, processed, fabricated, or packages for use by infants, children, or adults.
- Tampons, sanitary napkins, menstrual cups, and menstrual sponges.

Also beginning January 1, 2018 at 2:01am, this bill imposes an additional surtax on distilled spirits at the following rates:

- \$1.20 per wine gallon for distilled spirits 100 proof or less.
- \$2.40 per wine gallon for distilled spirits over 100 proof.

This bill also imposes equivalent floor stock taxes on all distilled spirits that are in the possession or under control of every person required to hold an alcoholic beverage license⁷ at 2:01am on January 1, 2018. Distilled spirits manufacturers, manufacture’s agents, brandy manufacturers, rectifiers, wholesalers, or common carriers licensed to sell distilled spirits on board boats, trains, and airplanes are exempt from imposing the floor stock tax. The taxes are due and payable to the BOE on or before February 15, 2018. The floor tax return shall contain the amount of units of distilled spirits in possession by the taxpayer on January 1, 2018 that are subject to the surtax imposed by this bill, and any other information the BOE deems necessary.

As a tax levy, the bill is effective immediately, but is operative on January 1, 2018.

⁶ Sections 32151, 32201, and 32220 of Part 14 (commencing with Section 32001) of Division 2 of the RTC.

⁷ Chapter 3 or Division 9 of Business and Professions Code (commencing with section 23300).

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Background: In 2016, Governor Brown vetoed a package of bills that would have created new tax breaks or expanded existing tax breaks worth hundreds of millions of dollars. Two of the bills vetoed by Governor Brown would have exempted from sales tax both diapers used by infants and toddlers, and feminine hygiene products. Governor Brown’s veto message stated, “Each of these bills creates a new tax break or expands an existing tax break. In total, these bills would reduce revenues by about \$300 million through 2017-18.” In a [news release](#), Governor Brown stated, “As I said last year, tax breaks are the same as new spending – they both cost the General Fund money. As such, they must be considered during budget deliberations so that all spending proposals are weighed against each other at the same time. This is even more important when the state’s budget remains precariously balanced. Therefore, I cannot sign these measures.”

Legislative History: The following are recent measures to exempt diapers or feminine hygiene products and increase taxes on alcoholic beverages.

Feminine Hygiene Products:

Year	Bill	Summary
2016	AB 1561	Proposed sales and use tax exemption on feminine hygiene products, with a five year sunset date. This bill was vetoed by Governor Brown along with six other tax exemption bills.

Diapers:

Year	Bill	Summary
2016	AB 717	Proposed sales and use tax exemption on diapers for use by infants and toddlers, with a five year sunset date. This bill was vetoed by Governor Brown along with six other tax exemption bills.
2001	AB 1291	Proposed sales and use tax exemption on diapers for use by infants and toddlers, with a five year sunset date. Died in the Assembly Revenue and Taxation Committee.
1999	AB 5	Proposed sales and use tax exemption for baby diapers and over-the-counter, nonprescription drugs. Failed in the Assembly Revenue and Taxation Committee.
1999	AB 13	Proposed sales and use tax exemption for over-the-counter, nonprescription, non-herbal medicines that are for internal use, and incontinence products, including disposable and reusable diapers, pads, and briefs. Failed in the Assembly Revenue and Taxation Committee.

Alcoholic Beverage Taxes:

Year	Bill	Summary
2010	AB 1694	Proposed a per gallon mitigation fee on beer, wine, and distilled spirits sold at resale by an alcoholic beverage seller. Failed in the Assembly Health Committee.
2009	SBx1 1	Proposed an additional surtax per gallon on beer (\$0.53), wine (\$1.28), and distilled spirits (4.27). Failed on the Assembly Floor.
2009	AB 1019	Proposed a per gallon mitigation fee on beer, wine, and distilled spirits sold at resale by an alcoholic beverage seller, as defined. Failed in the Assembly Health Committee.
2002	AB 2744	Proposed an alcohol beverage surtax increase. Failed in the Assembly Health Committee.

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Commentary:

1. **Effect of the bill.** Exempts from sales and use tax the sales and purchases of specified feminine hygiene product and diapers. To offset the revenue loss, this bill increases the distilled spirits surtax.
2. **Certain care providers, hospitals, and services would additionally benefit from the proposed exemption.** Since sales of menstrual products and diapers to these service enterprises are currently subject to tax, this bill would provide an additional benefit to entities that purchase these products for their clients or patients.
3. **The bill has no income or use limitations.** Women, adults, and parents of all income levels would receive the benefit of the exemption.
4. **This exemption does not include all menstrual products.** Tax would still apply to products like period panties and reusable cloth pads.
5. **The revenue generated from the surtax would only cover a portion of the revenue lost from the exemptions.** The proposed distilled spirits surtax is estimated to generate \$80 million in Fiscal Year (FY) 2018-19 for deposit in the General Fund. Conversely, the estimated revenue loss from the exemptions would be approximately \$139 million in FY 2018-19. Since the alcohol beverage surtax is deposited into the General Fund, the overall \$59 million revenue shortfall would primarily impact the Local Public Safety Fund, the Local Revenue Funds, Bradley-Burns local taxes to cities and counties, and the varies local district tax funds. (see page 5 Revenue Estimate for details)
6. **A delayed operative date of July 1, 2018 is suggested.** To effectively implement the floor tax and additional surtax on distilled spirits, the BOE must identify and notify taxpayers; develop computer programs; train key staff; create necessary forms and returns; and answer taxpayer inquires. These activities must take place before the tax becomes operative.

The BOE is currently in the implementation stage of replacing its legacy computer system. The new system, known as the Centralized Revenue Opportunity System ([CROS](#)), is due for its first roll out in April 2018. The CROS project involves extensive reconfiguring of the BOE's primary tax administration system. The implementation and stabilization efforts will occupy significant BOE staff resources for the rest of 2017, and into 2020.

In addition, the BOE is implementing new tax programs under [Proposition 56](#) (Cigarette and Tobacco Tax Law), [Proposition 64](#) (Marijuana Tax Law), and [AB 2153](#) (Lead Acid Battery Fee), and other legislative mandates including [ABx2 11](#) (Cigarette and Tobacco Products Licensing Act fees), AB 1245 (New Employment Registry Program), and [AB 1717](#) (Prepaid Mobile Telephony Services Surcharge). Based on both lack of available human resources and bandwidth, the BOE could not administer a new tax or fee program or make other significant programming changes before July 1, 2018, without substantial risk to legislative and voter approved mandates and other projects currently in process.

7. **Administrative start-up cost funding is essential.** The bill increases the alcoholic beverage tax on and after January 1, 2018. As a result, the BOE must begin to implement the bill in FY 2017-18. However, the BOE's 2017-18 budget does not include funding to implement the bill. Consequently, the BOE requires an adequate appropriation to cover administrative implementation costs.
8. **Related legislation.** [Assembly Bill 9](#) (C. Garcia) exempts from the sales and use tax the same feminine hygiene products as proposed by this bill.

Costs: BOE would incur costs to implement the additional distilled spirit surtax and floor tax. These costs would include: notifying affected retailers and taxpayers, answering inquiries, creating a floor tax return, reconciling and verifying returns, conducting audits, issuing billings and computer programing. A cost estimate of this workload is pending.

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Revenue Impact:

Surtax on Distilled Spirits. Based on BOE’s distilled spirits gallons data and the proposed surtax rates, a January 1, 2018 operative date yield the following estimated revenues:

	Surtax Revenue	Sales Tax on Surtax	Total Surtax Revenue Gain
FY 2017-18*	\$42,000,000	\$3,000,000	\$45,000,000
FY 2018-19	\$74,000,000	\$6,000,000	\$80,000,000

*FY 2017-18 reflects a half year impact and the proposed floor stock tax.

Feminine Hygiene Products. According to IBISWorld, a global business intelligence leader specializing in industry market research, the sanitary paper product manufacturing industry produces hygienic paper goods, including toilet paper, paper towels, facial tissues, diapers, menstrual pads and tampons. In FY 2017-18, U.S industry revenues are estimated to be \$10.8 billion. An estimated 20.3% of the industry represents feminine products segment which is composed of tampons and menstrual pads. Hence, feminine industry revenues are estimated to be \$2.2 billion (20.3% × \$10.8 billion = \$2.2 billion).

Based on California’s population, staff estimated feminine industry revenues in California to be \$264 million (\$2.2 billion × 12% = \$264 million).

Operative January 1, 2018, staff estimates that sales and use tax loss in FY 2017-18 will be \$21.6 million (8.21% statewide average × \$264 million = \$21.6 million). The half year fiscal effect is therefore \$10.8 million. Sales and use tax loss in FY 2018-19 is estimated to be \$21.7 million. The following is a breakdown:

Feminine Hygiene Products - Sales & Use Tax Exemption Impact

		FY 2017-18 (6 months)	FY 2018-19
State (Basic)	3.94%	\$5,150,000	\$10,500,000
Local Revenue 2011	1.06%	\$1,400,000	\$2,800,000
Local Revenue 1991	0.50%	\$650,000	\$1,300,000
Public Safety Fund	0.50%	\$650,000	\$1,300,000
Bradley Burns	1.25%	\$1,650,000	\$3,300,000
Special District	0.96%	\$1,250,000	\$2,500,000
Statewide Average Rate	8.21%	\$10,750,000	\$21,700,000

Diapers – Children and Adults. Industry data indicate adult diapers to be a \$1.5 billion industry. Based on California’s population, staff estimated adult diaper industry revenues in California to be \$180 million (\$1.5 billion × 12% = \$180 million). Staff estimated infant and toddler diaper industry revenues to be \$1.2 billion.

Operative January 1, 2018, staff estimates that sales and use tax loss in FY 2017-18 will be \$58.5 million (half year fiscal effect). Sales and use tax loss in FY 2018-19 is estimated to be \$117.7 million. The following is the breakdown:

Adult & Infant/Toddler Diapers - Sales & Use Tax Exemption Impact

		FY 2017-18 (6 months)	FY 2018-19
State (Basic)	3.94%	\$28,069,000	\$56,473,000
Local Revenue 2011	1.06%	\$7,574,000	\$15,239,000
Local Revenue 1991	0.50%	\$3,564,000	\$7,170,000
Public Safety Fund	0.50%	\$3,564,000	\$7,170,000
Bradley Burns	1.25%	\$8,911,000	\$17,928,000
Special District	0.96%	\$6,844,000	\$13,769,000
		\$58,526,000	\$117,749,000

Revenue Summary. The proposed surtax on distilled spirits is estimated to generate \$45 million in FY 2017-18 and \$80 million FY 2018-19.

The proposed sales and use tax exemption on feminine products and diapers would result in estimated sales and use tax loss of \$69 million in FY 2017-18. In FY 2018-19, the revenue loss is estimated to be \$139 million.

The following is the revenue impact breakdown:

	Revenue Impact	
	FY 2017-18 (6 month impact)	FY 2018-19
Surtax on Distilled Spirits	\$45,000,000	\$80,000,000
Sales & Use Tax Exemptions	<u>(\$69,000,000)</u>	<u>(\$139,000,000)</u>
Net Revenue	(\$24,000,000)	(\$59,000,000)

Qualifying Remarks. The basis for the sales and use tax exemption for feminine hygiene products revenue estimate is the IBISWorld feminine products segment data. The segment is composed of tampons and menstrual pads. Staff understands this segment receives competition from alternative feminine products that is probably not captured in the above data. Hence, the revenue estimate may be understated.

This revenue estimate does not account for any changes in economic activity that may or may not result from enactment of the proposed law.