California State Board of Equalization,
Legislative and Research Division

LEGISLATIVE BULLETIN

State Capitol Building (from the East) c.1945
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SALES TAX LEGISLATION
2013

SALES TAX LEGISLATION
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Assembly Bill 92 (Committee on Budget) Chapter 26

Triple Flip Sunset

Effective June 27, 2013. Among other things, amends Section 97.68 of the Revenue and Taxation Code.

BILL SUMMARY

Among its provisions, this budget trailer bill prepares for the end of the "Triple Flip" by outlining a process to provide final compensation to cities and counties for their 0.25% local sales and use tax revenue loss after the Economic Recovery Bonds are paid off. The bill also requires the Director of Finance (DOF) to estimate when it likely will notify the BOE of the pay-off, and revise the countywide adjustment amount upon notification.

Sponsor: Committee on Budget

LAW PRIOR TO AMENDMENT

On March 2, 2004, voters approved Proposition 57, the Economic Recovery Bond Act (Act),[1] which became operative July 1, 2004, and authorized the issuance of up to $15 billion in bonds to finance the accumulated budget deficit.

The Act[2] also increased the statewide sales and use tax rate by 0.25% and decreased by a like amount the Bradley-Burns Uniform Local Sales and Use Tax rate (cities and counties are reimbursed for their local tax revenue losses through property tax revenues). The resulting 0.25% state sales and use tax revenue is deposited into the Fiscal Recovery Fund and dedicated to the repayment of the deficit reduction bonds.

Current law[3] provides that cities and counties are reimbursed for the 0.25% local sales tax rate reduction through property tax revenues from the Educational Revenue Augmentation Fund (ERAF). By September 1 of each fiscal year, the DOF, in conjunction with the BOE, prepares an annual estimate of the local sales and use tax revenue losses attributable to the reduction in the local sales and use tax rate. This estimate, known as the "countywide adjustment amount," is based on prior fiscal year transmittals (also referred to as distributions) of actual local sales and use tax revenue. Cities and counties receive property tax replacement revenue twice per year—in January and May. At the end of each fiscal year, the property tax replacement revenue is reconciled with the actual local sales and use tax revenue *not* transmitted as a result of the 0.25% local sales and use tax rate reduction.

In addition, Section 97.68 defines "fiscal adjustment period" as the period beginning with the 2004-05 fiscal year and continuing through the fiscal year in which, pursuant to Government Code (GC) Section 99006, the DOF notifies the BOE that the $15 billion Economic Recovery Bonds (ERBs) have been paid or the Fiscal Recovery Fund holds sufficient funds to retire them. Section 97.68 also specifies how to allocate the countywide adjustment amount after the end of the fiscal adjustment period.

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[1] Assembly Billx5 9, Chapter 2, Statutes of 2003-04 Fifth Extraordinary Session.
[2] Revenue and Taxation Code (RTC) Sections 6051.5 and 6201.5 of the Sales and Use Tax Law and RTC Section 7203.1 of the Bradley-Burns Uniform Local Sales and Use Tax Law.
[3] RTC Section 97.68 of the Property Tax Law.

AMENDMENT

This bill prepares for the end of the triple flip by providing final compensation to cities and counties once the mechanism is no longer needed to repay the ERBs. Specifically, this bill:

- Redefines the "fiscal adjustment period" to instead mean the fiscal year in which the DOF notifies the BOE pursuant to subdivision (b) of GC Section 99006, or the fiscal year in which the DOF determines an additional countywide adjustment amount, whichever is later.
- Requires the DOF to estimate when it likely will notify the BOE within the subsequent 12 months and to determine the month in which the notification will occur at the beginning of each subsequent calendar year quarter.
- Requires the DOF, in the calendar year quarter when the DOF determines that the notification to the BOE will occur within either the current or subsequent quarter, to revise the countywide adjustment amount for the current fiscal year such that the countywide adjustment amount is calculated only through the quarter in which DOF gives the notification.
- Requires the DOF to provide to the Controller and the Joint Legislative Budget Committee, after the end of the revenue exchange period,[4] a schedule of the amounts needed to fully compensate cities and counties for the revenue they did not receive as a result of the 0.25% reduction in the local sales and use tax rate.
- Requires the Controller to transfer the amounts specified in the schedule from the Fiscal Recovery Fund to the Sales and Use Tax Compensation Fund in each county for allocation by the county auditor to each county and each city in the county.

This bill takes effect immediately as a bill related to the 2013 Budget Act.

LEGISLATIVE HISTORY

Governor Gray Davis signed the original Triple Flip bills, Assembly Bill x1 7 (Chapter 13, Statutes of 2003-04 First Extraordinary Session) and Assembly Bill 1766 (Chapter 162, Statutes of 2003) on August 2, 2003, as part of the 2003-04 Budget Plan. AB x1 7 enacted the California Fiscal Recovery Financing Act and authorized the issuance of $10.7 billion in bonds to finance the cumulative fiscal year 2002-03 budget deficit. These bonds were never issued and the "triple flip" bills never became operative due to a legal challenge.

On December 12, 2003, Governor Schwarzenegger signed Assembly Bill x5 9 (Chapter 2, Statutes of 2003-04 Fifth Extraordinary Session), which enacted the Economic Recovery Bond Act and authorized the issuance of up to $15 billion in bonds to finance the accumulated budget deficit. AB x5 9 reduced the tax rates proposed under the original Triple Flip bills[5]) The voters approved Governor Schwarzenegger's $15 billion bond measure (Proposition 57) on March 2, 2004, and it became operative July 1, 2004.

[4] Revenue exchange period, as defined in RTC Section 7203.1, means the period on and after July 1, 2004, and before the first day of the first calendar quarter commencing more than 90 days following DOF's notification to the BOE pursuant to subdivision (b) of GC Section 99006.

[5] It repealed and added specified statutes that were originally enacted under AB x1 7 and AB 1766.

COMMENTS

1. **Purpose.** This budget trailer bill contains the necessary statutory changes to implement the 2013 Budget Act related to general government. Among its provisions, it prepares for the end of the Triple Flip by outlining a process to provide final compensation to cities and counties once the mechanism is no longer needed to pay for the ERBs.

2. **The bill would not change the timing to "turn off" the Triple Flip under current sales and use tax law.** RTC Sections 6051.5, 6201.5, and 7203.1 provide that the 0.25% state sales and use tax rate (dedicated to repay the ERBs) will cease and the 0.25% local sales and use tax rate will be restored *on the first day of the first calendar quarter commencing more than 90 days following a notification to the BOE by the DOF pursuant to subdivision (b) of GC Section 99006* (when there is sufficient revenue in the Fiscal Recovery Fund to pay off the economic recovery bonds). Under this budget trailer bill, BOE staff would still have 90 days to turn off the Triple Flip. According to the LAO report, *Summary of LAO Findings and Recommendations on the 2013-14 Budget*, the 2013-14 Governor's Budget expects the economic recovery bonds to be repaid in June 2016. If that estimate is accurate, the triple flip would turn off on October 1, 2016, under current statutes.

3. **This measure corrects an unintended consequence of the enabling legislation.** Because of a lag between the time when taxable sales are reported to the BOE and when those amounts are distributed to each city and county, those entities were only compensated for the first three quarters of the Triple Flip's first year (2004-05). Every subsequent year, however, cities and counties have been compensated for a full four quarters. The compensation has been based on distributions that took place between April 1 of the prior fiscal year to March 31 of that fiscal year. In other words, the July 1 to June 30 fiscal year compensation is based on April 1 to March 31 distributions.

   The 2013-14 Governor's Budget estimates the ERBs to be repaid in June 2016, while the Triple Flip will expire October 1, 2016. At this point, the existing Triple Flip mechanism should have provided for cities and counties to be reimbursed for the 0.25% local sales and use tax revenue loss through March 31, 2016m. Therefore, the cities and counties would need to be compensated for another two quarters (April 1, 2016 through September 30, 2016). However, current Section 97.68 only authorizes reimbursement for the first quarter of the current fiscal year (July 1, 2016 through September 30, 2016). Without addressing this issue, cities and counties will fall short of compensation for one quarter—April 1, 2016 through June 30, 2016. A similar shortfall would occur regardless of which calendar quarter the 0.25% rate is restored to cities and counties.

4. **BOE staff has no administrative concerns.** This budget trailer bill makes several changes related to preparing for the end of the triple flip. As explained under comment #3, the original trip flip statute did not contemplate the one quarter lag between the date a taxable sale is reported and the date by which the BOE has sufficient data to determine the correct amount to distribute to cities and counties. This bill provides a method to correct that.

Assembly Bill 143 (Holden) Chapter 687

Use Tax Exemption: Military Transfers

Tax levy; effective October 10, 2013, but operative on April 1, 2014. Adds and repeals Section 6412 of the Revenue and Taxation Code.

BILL SUMMARY

This bill exempts U.S. Armed Forces members, U.S. Armed Forces and National Guard active duty reserves, their spouses, and registered domestic partners from use tax on specified purchases of tangible personal property. The exemption applies to purchases of tangible personal property made outside California prior to the report date on official transfer orders transferring him or her to this state. This exemption specifically excludes vehicles, vessels, and aircraft and sunsets on January 1, 2019.

Sponsor: Assembly Member Holden

LAW PRIOR TO AMENDMENT

Existing California law[1] imposes a use tax on the storage, use, or other consumption in this state of tangible personal property purchased from any retailer. The use tax is imposed at the same rate as the sales tax. Purchasers are liable for the use tax. They must pay the tax to the state unless they have a receipt proving that they paid the tax to a retailer registered to collect the California use tax. Retailers engaged in business in California and/or registered to collect the California use tax must collect the use tax from the purchaser at the time of purchase and remit the tax to the state.

When a California consumer or business purchases tangible items for their own use from an out-of-state retailer that is not registered with the Board of Equalization (BOE) to collect the California use tax, the purchaser must remit the use tax to the BOE. Generally, purchasers must remit the use tax to the BOE on or before the last day of the month following the quarterly period in which they made the purchase. As an alternative to reporting the use tax directly to the BOE, existing law allows purchasers to report use tax on their state personal income tax returns or their state corporation franchise or income tax returns.

California law regards property purchased outside of California as purchased for use in this state if the first functional use of the property is in California. When property is first functionally used outside California, existing California law nevertheless presumes that it is purchased for use in this state if it is brought into California within 90 days of purchase, unless the purchaser uses or stores the property outside California one-half or more of the time during the six-month period immediately following its entry into this state.

Revenue and Taxation Code Section 6406 allows a credit against, but not exceeding, the use tax to the extent that the person has paid a retail sales or use tax on the property in another state, political subdivision thereof, or the District of Columbia prior to the property's storage, use or other consumption in California.

[1] Chapter 3 (commencing with Section 6201) of Part 1 of Division 2 of the Revenue and Taxation Code.

AMENDMENT

This bill adds and repeals Revenue and Taxation Code Section 6412 of the Sales and Use Tax Law to exempt from use tax tangible personal property purchased by qualified service members or their spouse or registered domestic partner , provided they purchased the property:

1. When they were outside the state; and
2. Prior to the report date on official orders transferring them to this state.

The bill defines the following terms:

“Qualified service member” means a member of the Armed Forces on active duty or a member of a reserve component of the Armed Forces of the United States, or a member of the National Guard on active duty.

“Qualified tangible personal property” means tangible personal property other than a vehicle, vessel, or aircraft.

As a tax levy, this bill takes immediate effect. However, the provisions become operative on the first day of the first calendar quarter commencing more than 90 days after the effective date. This new section sunsets on January 1, 2019.

COMMENTS

1. **Purpose.** This bill intends to relieve active duty military service members of unexpected use tax they may incur when the military requires them to relocate to serve our country.
2. **Vehicles.** Currently, active duty armed services members need not pay the use tax on vehicle purchases when (1) the service member purchases the vehicle outside California, and (2) the service member’s intent to use the vehicle in California results from official transfer orders to California and not from the service member’s own independent determination.
3. **Administration.** BOE staff does not anticipate any administrative complications from this measure.

Assembly Bill 163 (Atkins) Chapter 72

Military Thrift Stores Exemption

Tax levy; effective August 12, 2013. Amends Section 6363.4 of the Revenue and Taxation Code.

BILL SUMMARY

This bill extends from January 1, 2014 to January 1, 2024 the sunset date applicable to the sales and use tax exemption for specified military-related nonprofit thrift store sales.

Sponsor: Navy Region Southwest

LAW PRIOR TO AMENDMENT

Except where the law provides a specific exemption or exclusion, California's Sales and Use Tax Law[1] 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.

The law does not generally exempt from tax sales or purchases by nonprofit organizations, sellers or purchasers engaged in charitable activities, or those who enjoy certain income tax or property tax privileges. However, several specific statutes benefit various nonprofit groups engaged in charitable activities. For example, the law[2] exempts specific military-related thrift store sales from the sales and use tax until January 1, 2014. This section provides that thrift store sales are exempt from sales and use tax when nonprofit organizations operate the thrift stores on military installations and partner with the United States Department of Defense to provide financial, educational, and other assistance to United States Armed Forces members, eligible family members, and survivors in need.

Other provisions in law also exempt specified nonprofit thrift store sales from the sales and use tax. For example, a nonprofit organization's thrift store sales of used clothing, household items, or other retail items are exempt from sales and use tax when the thrift store's purpose is to obtain medical, hospice, or social services funding for chronically ill individuals, as specified and defined.

Another exemption[3] applies to charitable organizations' sales if the organization qualifies for the property tax "welfare exemption."[4] To be exempt, the law requires that (1) the organization relieves poverty and distress; (2) the sales principally assist financially distressed purchasers; and (3) the organization makes, prepares, assembles, or manufactures the property sold. For example, Goodwill's and Salvation Army's thrift store sales qualify for this sales and use tax exemption because their thrift store premises qualify for the "welfare exemption," and they meet the other requirements in law.

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[1] Part 1 (commencing with Section 6001) of. Division 2 of the Revenue and Taxation Code (RTC).
[2] RTC Section 6363.4 of the Sales and Use Tax Law.
[3] RTC Section 6375 of the Sales and Use Tax Law.
[4] RTC Section 214 of the Property Tax Law.

AMENDMENT

This bill amends Section 6363.4 to extend from January 1, 2014 to January 1, 2024, the sunset date on the sales and use tax exemption for military-related thrift store sales.

The bill takes effect immediately.

BACKGROUND

In 2009, Senate Bill 765[5] added Sales and Use Tax Law Section 6363.4. All Board of Equalization (BOE) Members voted unanimously to sponsor SB 765 at the December 8, 2008 BOE Legislative Committee meeting. The BOE Members supported this narrowly crafted exemption with no sunset date, as they believed our service members and their families should not bear the additional sales tax expense added to their thrift store purchases. At the SB 765 legislative hearing, the Assembly Revenue and Taxation Committee added the sunset date.

Section 6363.4 applies to military welfare societies from all branches of the military. However, we understand that only the Navy-Marine Corps Relief Society (NMCRS) operates thrift stores.

Operating in partnership with the Navy and Marine Corps, the NMCRS is a nonprofit, charitable organization that qualifies for federal and state income tax exempt status.[6] The NMCRS provides financial, educational, and other assistance to U.S. Naval Services members and their eligible family members and survivors in need. To assist in relief services, the NMCRS operates 27 thrift stores, including seven at California Naval or Marine bases in San Diego, Barstow, Miramar, Camp Pendleton, Port Imperial Beach, Ventura, and Lemoore. These thrift stores sell nominally-priced used clothing, uniforms, and household items to service members and their families. The thrift stores' sales income partly supports relief services to the Navy-Marine Corps community.

COMMENTS

1. **Purpose.** The Navy Region Southwest sponsored this bill. According to the author's office, the NMCRS thrift stores provide an important service that supports military families. Maximizing the amount of money that assists veterans and active duty personnel is a small acknowledgment of the many sacrifices they have made for their fellow Californians.
2. **Who shops at these thrift stores?** Located on military bases and closed to the general public, the NMCRS allows only military families and Department of Defense employees, including retirees and civilian contractors, to patronize these thrift stores.

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[5] Dutton, Ch. 615, Stats. 2009.

[6] Title 26, Section 501(c)(3) of the United States Code for federal income tax purposes, and RTC 23701d for state income tax purposes.

Assembly Bill 210 (Wieckowski) Chapter 194

Transactions and Use Tax – Alameda and Contra Costa Counties

Effective January 1, 2014. Amends Sections 7291 and 7292 of the Revenue and Taxation Code.

BILL SUMMARY

This bill extends the authority of Alameda County, and authorizes Contra Costa County, to impose a countywide transportation program transactions and use tax (district tax), until December 31, 2020. The tax may exceed the existing 2% rate limitation.

Sponsor: Alameda County

LAW PRIOR TO AMENDMENT

The State Board of Equalization (BOE) administers locally-imposed sales and use taxes under the Bradley-Burns Uniform Local Sales and Use Tax Law and under the Transactions and Use Tax Law. By law, cities and counties (and special purpose entities) contract with the BOE to administer the ordinances imposing the local and district taxes.

The **Bradley-Burns Uniform Local Sales and Use Tax Law**[1] authorizes cities and counties to impose local sales and use tax. This tax rate is fixed at 1% of the sales price of tangible personal property sold at retail in the local jurisdiction, or purchased outside the jurisdiction for use within the jurisdiction. Of this 1%, cities and counties use 0.75% to support general operations. The remaining 0.25% is designated by statute for county transportation purposes, but restricted for road maintenance or the operation of transit systems. The counties receive the 0.25% tax for transportation purposes regardless of whether the sale occurs in a city or in the unincorporated area of a county. In California, all cities and counties impose Bradley-Burns local taxes at the uniform rate of 1%.

The **Transactions and Use Tax Law**[2] and the **Additional Local Taxes Law**[3] authorize cities, counties, and special purpose entities to impose district taxes under specified conditions. Counties may impose a district tax for general purposes and special purposes at a rate of 0.125%, or multiples thereof, if the ordinance imposing the tax is approved by the required percentage of voters in the county. Cities also may impose a district tax for general purposes and special purposes at a rate of 0.125%, or multiples thereof, if the ordinance imposing the tax is approved by the required percentage of voters in the city. The combined district tax rate imposed within any local jurisdiction, except Los Angeles County,[4] cannot exceed 2%.[5]

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[1] Part 1.5 (commencing with Section 7200) of Division 2 of the Revenue and Taxation Code (RTC).
[2] Part 1.6 (commencing with Section 7251) of Division 2 of the RTC.
[3] Part 1.7 (commencing with Section 7280) of Division 2 of the RTC.
[4] In 2003, SB 314 (Chapter 785, Murray) authorized the Los Angeles Metropolitan Transportation Authority to impose a 0.50% district tax for specific transportation projects, and excluded that 0.50% tax from the 2% combined rate limitation established by RTC 7251.1. In 2008, voters within Los Angeles County approved the additional 0.50% effective July 1, 2009, which raised the tax rate in the cities of South Gate and Pico Rivera to 10%. Effective April 1, 2013, the tax rate in the City of La Mirada (in Los Angeles County) also will be 10%.
[5] RTC Section 7251.1.

In addition, Section 7291 authorizes Alameda County to impose a district tax for transportation programs at a capped rate of 0.50%,[6] provided all of the following conditions are met:

(1) Alameda County adopts an ordinance proposing the district tax by any applicable voting requirements;

(2) the proposed ordinance is submitted to the electorate on the November 6, 2012, general election ballot and is approved by two-thirds of the voters voting on the ordinance; and,

(3) the district tax conforms to the Transactions and Use Tax Law.

If the ordinance is not approved by the electorate by November 6, 2012, Section 7291 will be repealed as of January 1, 2014.

AMENDMENT

This bill extends Alameda County's authority, and grants Contra Costa County the authority, to impose a district tax for countywide transportation programs until December 31, 2020. The bill deletes the requirement that the ordinance be submitted to the voters on the November 6, 2012, general election ballot. However, the proposed district tax ordinance must be approved by the voters as of December 31, 2020, or the bill's provisions will be repealed as of that same date.

The bill states that the Legislature finds and declares that a special law is necessary because of the unique fiscal pressures experienced in Alameda County and Contra Costa County in providing essential transportation programs.

The bill takes effect on January 1, 2014.

BACKGROUND

Assembly Bill 1086 (Wieckowski, Ch. 327, Stats. 2011) enacted the statutory authorization for Alameda County to impose a district tax for transportation purposes that is excluded from the 2% rate limitation. The bill required that the ordinance proposing the tax be submitted to the electorate on the November 6, 2012, general election ballot. Failure to enact the ordinance by that date will result in the statute's sunset on January 1, 2014.

Alameda County voters declined to approve the proposed district tax (Measure B1) on the November 6, 2012, ballot; the measure fell 0.14% short of the 66.6% super-majority needed to pass.

DISTRICT TAXES CURRENTLY ADMINISTERED BY THE BOE

Beginning April 1, 2013, there will be 169 local jurisdictions (city, county, and special purpose entity) imposing a district tax for general or specific purposes. Of the 169 jurisdictions, 43 are county-imposed taxes and 126 are city-imposed taxes. Of the 43 county-imposed taxes, 28 are imposed for transportation purposes.

Currently, the district tax rates vary from 0.10% to 1%. The combined state, local and district tax rates range from 7.625 to 9.50%, with the exception of the cities of La Mirada, Pico Rivera, and South Gate (10%) in Los Angeles County.

[6] In combination with other district taxes, this amount exceeds the 2% limitation established under existing law.

A listing of the district taxes, rates, and effective dates is available on the BOE's website: www.boe.ca.gov/sutax/pdf/districtratelist.pdf.

COMMENTS

1. **Purpose.** This bill intends to provide additional funding for transportation programs and services for the counties of Alameda and Contra Costa. According to the author's office, in November 2010, voters within the city of Union City approved an additional 0.5% tax, effective April 1, 2011. Consequently, Alameda County cannot enact a new district tax; Union City's 0.5% tax, combined with the county's district taxes, already reaches the maximum 2% limit.

   Similarly, in November 2012, voters within the city of Moraga approved an additional 1% tax effective April 1, 2013. Thus, a new county-wide tax also would push Contra Costa County over the 2% limit.

2. **Current district taxes levied within Alameda and Contra Costa Counties.** Currently, **Alameda County** has five district taxes imposed within its borders—three county-wide taxes and two city-wide taxes. The three county-wide taxes have 0.50% tax rates, for a total county-wide tax rate of 1.50%. Thus, the total state, local, and district tax rate imposed within the unincorporated area of Alameda County is 9%. The two cities that impose a district tax are San Leandro, at a rate of 0.25% and Union City, at a rate of 0.50%, with a total state, local, and district tax rate of 9.25% and 9.50%, respectively.

   As previously stated, cities and counties may impose district taxes as long as the combined rate does not exceed 2% within the county. The city district taxes count against the 2% limit. Because Union City imposes a tax of 0.50%, Alameda County may not enact a new district tax without this bill.

   Of the three county-wide taxes, two are imposed for transportation purposes, and one is imposed for essential health care services. The Alameda County Transportation Improvement Authority (ACTIA) and the Bay Area Rapid Transit levy two 0.50% district transportation taxes. In 2010, the ACTIA merged with the Alameda County Congestion Management Agency (ACCMA) to form the new county-wide transportation agency—the Alameda County Transportation Commission (Alameda CTC). The Alameda CTC is a joint powers authority whose members include the 14 cities in Alameda County, the County of Alameda, Alameda County Transit, BART, ACCMA, and ACTIA.

   Currently, **Contra Costa County** has twelve district taxes imposed within its borders—two county-wide taxes and ten city-wide taxes. BART and Contra Costa County Transportation Authority (CCTA) each levy 0.5% transportation-related taxes for a total county-wide tax rate of 1%. Thus, the total state, local and district tax rate imposed within the unincorporated area of Contra Costa County is 8.50%.

   Eight cities impose a 0.5% district tax (Concord, Hercules, Orinda, Pinole, Pittsburg, Richmond, and San Pablo), while El Cerrito[7] and Moraga impose 1% taxes. The overall tax rates in these cities are 9 and 9.5%, respectively.

[7] The City of El Cerrito levies two district taxes: a 0.5% tax for general purposes and another 0.5% tax for street improvements.

3. **Other California counties at or near the 2% limit.** San Mateo County has reached the 2% limit with its three 0.5% county-wide taxes (1.5%) and two city-wide taxes (Half Moon Bay (0.5%) and San Mateo (0.25%)). Because Half Moon Bay imposes a 0.5% tax, San Mateo County has reached the 2% limit.

   While San Diego County only levies one 0.5% district tax, five cities impose their own. National City's 1% rate leaves San Diego County 0.5% shy of the 2% limit.

Assembly Bill 576 (V. Perez) Chapter 614

Revenue Recovery and Collaborative Enforcement Team Act

Effective January 1, 2014. Adds and repeals Part 12.2 (commencing with Section 15910) of Division 3 of Title 2 of the Government Code.

BILL SUMMARY

This bill creates a multiagency team among the Board of Equalization (BOE), Franchise Tax Board (FTB), Employment Development Department (EDD) and the Department of Justice (DOJ) to combat criminal tax evasion related to underground economic activity. The Revenue Recovery and Collaborative Enforcement (RRACE) Team authorizes members and other participating agencies to exchange information for the purpose of investigating underground operations that are evading state taxes. This bill formalizes information sharing and communication regarding criminal tax evasion among participating agencies.

Sponsor: Board of Equalization

LAW PRIOR TO AMENDMENT

Joint agency enforcement programs are established in law to combat the underground economy. These include the Joint Enforcement Strike Force (JESF) and the Labor Enforcement Task Force (LETF). Additional agency efforts include the BOE's Statewide Compliance and Outreach Program and the Contractor State License Board's Statewide Investigative Fraud Team.

AMENDMENT

The bill adds and repeals Part 12.2 (commencing with Section 15910) to Division 3 of Title 2 of the Government Code to establish the RRACE Team as a pilot program. The proposed Team includes the BOE, FTB, EDD and DOJ, which will work cooperatively to pursue criminal tax evasion resulting from underground economic activities.. This bill authorizes members of the Team and other participating agencies to exchange information for the purpose of investigating underground operations that result in state tax evasion. The RRACE Team will investigate organized criminal entities and/or serial offenders for violation of tax laws.

The following agencies also may participate in the RRACE Team in an advisory capacity:

California Health and Human Services Agency

Department of Consumer Affairs

Department of Industrial Relations

Department of Insurance

Department of Motor Vehicles

Additionally, this bill:

- Allows authorized team representatives to exchange intelligence, data, documents, information, complaints, or lead referrals, related to criminal tax evasion associated with underground operations, notwithstanding any other law.

- Evaluates the benefits of a processing center to receive and analyze data, share complaints, and research leads from the input of each impacted agency.
- Develops a plan for a central intake process and organizational structure to document, review, and evaluate data and complaints.
- Provides participating and nonparticipating entities investigative leads to collaborate on felony-level criminal investigations.
- Requires the RRACE Team to provide a report to the Legislature by December 1, 2017, on the number of complaints processed and cases investigated or prosecuted, as a result of Team collaboration.

Funding is not provided in this bill. The scope of activities and projects undertaken will be consistent with the funds appropriated by the Legislature.

Governor's instructions. In his signing message, Governor Brown instructed the Department of Industrial Relations (DIR) to take the lead among the agencies to help avoid an overlap in efforts. He further instructed DIR to provide him recommendations to improve effectiveness in attacking the underground economy.

This statute sunsets on January 1, 2019.

BACKGROUND

The underground economy refers to those individuals and businesses that deal in cash and/or use other schemes to conceal their activities, identities and true tax liability. Activities range from the sale of stolen or counterfeit products to the exploitation of human trafficking victims.

Last year's SB 1185 (Price) proposed a Centralized Intelligence Partnership. That bill was held on the Assembly Appropriations Committee's suspense file.

COMMENTS

1. **Purpose.** The BOE supports the creation of the RRACE Team as a collaborative and strategic effort to combat tax evasion resulting from activities in the underground economy through comprehensive data and resource analysis. This collaborative effort is intended to significantly increase the efficiency and effectiveness of the BOE's efforts to recapture revenue lost to illegally operating businesses, thereby resulting in a more robust, legitimate economy.
2. **Tax evasion from the underground economy hurts all Californians.** Those who operate in the underground economy enjoy the same public services as tax and fee payers without making the same contributions.
3. **Current efforts focus on labor issues.** JESF and LETF focus primarily on labor issues. The BOE is an active member of both partnerships. However, due to the need to primarily pursue underground labor issues, JESF and LETF investigations have not resulted in significant criminal tax evasion leads. THE RRACE Team has the expertise and specific resources to focus only on criminal tax evasion.
4. **The RRACE Team will focus on criminal prosecution.** Minor and inadvertent violations by businesses will be addressed through other administrative procedures.

Assembly Bill 781 (Bocanegra) Chapter 532

Sales Suppression Devices: Prohibition

Effective January 1, 2014. Among its provisions, adds Section 7153.6 to the Revenue and Taxation Code.

BILL SUMMARY

This bill makes it a punishable offense for any person to knowingly sell, purchase, install, transfer or possess software programs that falsify reported sales, as specified.

Sponsor: Board of Equalization

LAW PRIOR TO AMENDMENT

Existing California law[1] sanctions taxpayers who intentionally fail to accurately report and remit tax and fee liabilities. In addition to a variety of civil penalties, the law imposes criminal penalties for violations. For example, any person who makes a fraudulent return with the intent to evade the determination of an amount due, or any person who assists in the preparation or presentation of a document that is false as to a material matter is guilty of a misdemeanor, punishable by a fine of at least $1,000 and not more than $5,000, or imprisonment up to one year in the county jail, or both the fine and imprisonment in the court's discretion. In addition, the law makes it a felony if the unreported tax liability is at least $25,000 in a consecutive 12-month period, punishable by a fine of at least $5,000 and not more than $20,000, or imprisonment for 16 months, or 2 or 3 years, or both the fine and imprisonment in the discretion of the court.

The existing Fee Collection Procedures Law[2] (FCPL) generally provides for the administration of fees collected by the Board of Equalization (BOE). Legislation that establishes a new fee may reference the FCPL with minimal verbiage. Among other things, this law includes collection, reporting, refund, and appeals provisions, and, similar to the Sales and Use Tax Law, provides criminal penalties for violations.

Existing law does not specifically penalize a person for the sale, purchase, installation, transfer, or possession of sales suppression devices or software that conceals or removes sales transactions from retailers' recordkeeping systems.

AMENDMENT

This bill makes it a misdemeanor for any person who purchases, installs, or uses in this state any specified sales suppression devices with the intent to defeat or evade the determination of an amount due.

In addition, the bill makes it a punishable offense for any person who, for commercial gain, purchases, installs, or uses in this state any specified sales suppression devices with the knowledge that the sole purpose of the device is to defeat or evade the determination of an amount due. The offense is punishable by a fine and/or imprisonment in the county jail for not more than one year, or for 16 months, or for two or three years. For a person guilty of selling, installing, transferring or possessing three or

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[1] Revenue and Taxation Code (RTC) Sections 7152 through 7157.

[2] Part 30 (commencing with Section 55001) of Division 2 of the RTC.

fewer sales suppression devices, a fine of up to $5,000 may be imposed. For a person who sold, installed, transferred, or possessed more than three sales suppression devices, a fine of up to $10,000 may be imposed.

The provisions do not apply to a person that is a corporation that possesses automated sales suppression devices or phantom-ware for the sole purpose of developing hardware or software to combat tax evasion by use of such devices or software.

The bill applies to the Sales and Use Tax Law, and the California Tire Fee and the Covered Electronic Waste Recycling Fee, which are fees imposed on consumers at the retail level and which are collected and administered under the FCPL.

The bill specifies that the person shall also be liable for the taxes and fees, interest, and penalties due.

The bill defines "automated sales suppression device," "zapper," "electronic cash register," "phantom-ware," and "transaction data."

BACKGROUND

California's tax system is based on voluntary compliance. Most tax or fee payers (taxpayers) who report taxes and fees to the BOE are honest and generally comply with the law. However, some seek to skim or hide their sales to evade the tax due. Some cash-based businesses, for example, ring up only a portion of their sales through their cash register, keep two sets of books, or simply file false tax returns.

Now, an electronic method to skim sales allows retailers to conceal or remove sales transactions from recordkeeping systems. These devices are referred to as "sales suppression devices," and the software is referred to as "phantom-ware." The use of this technology makes the detection of understated sales difficult in tax and fee audits.

COMMENTS

1. **Purpose.** As sponsors of this bill, the BOE Members believe that California must be proactive and curtail the sale and use of these sales suppression devices. Use of this technology not only defrauds the state, but also provides users an unfair competitive advantage over taxpayers who comply with the law and pay their fair share of taxes and fees. The Legislature has recognized through its enactment of criminal penalties for deliberate taxpayer fraud and evasion that criminal sanctions play an important role in tax administration. Specifically criminalizing and punishing the sale, installation, and use of sales suppression devices serves as a strong deterrent to potential manufacturers, sellers, installers, and users of these devices.
2. **Other states and Canada have banned these devices and software.** In 2011, Georgia became the first state to make it a crime to knowingly sell, purchase, install, transfer, or possess any automated sales suppression device or zapper or phantom-ware. Several other states have since enacted similar provisions, including Connecticut, Michigan, Louisiana, Maine, Tennessee, and West Virginia. Others, including Indiana and New York, have proposed legislation outlawing these devices and software. This year Canada enacted laws to impose fines and imprisonment for use, possession or acquisition of these sales suppression devices.
3. **Specific incidents of sales suppression software cases.** According to information obtained from the Federation of Tax Administrators' (FTA) website, examples of United States zapper cases involving substantial underreported sales include:

- Connecticut: The IRS discovered in an income tax audit that a grocery store had $17 million in underreported sales.
- Michigan: The CIA uncovered information from a restaurant chain owner's relative that the restaurant neglected to report $20 million in sales.
- Ohio: The FBI and the Joint Terrorism Task Force detected that a restaurant chain underreported $3 million in sales.
- New York: A *New York Post* article disclosed an undercover sting operation where 70% of electronic cash register sellers had tried selling zapper software with the systems they offered to potential customers.

Assembly Bill 1422 (Committee on Jobs, Economic Development, and the Economy) Chapter 540

California Alternative Energy and Advanced Transportation Financing Authority Exclusion: Participating Party

Effective January 1, 2014. Among other things, amends Section 26003 of the Public Resources Code.

BILL SUMMARY

This bill clarifies that an out-of-state or overseas entity can apply for a sales and use tax exclusion with the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) if that entity commits to, and demonstrates that, it will be opening a California manufacturing facility.

Sponsor: Committee on Jobs, Economic Development, and the Economy

LAW PRIOR TO AMENDMENT

Except where the law provides a specific exemption or exclusion, California's Sales and Use Tax Law[1] 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.

Generally, sales or use tax applies to the sale or purchase of tangible personal property to persons who use the property to manufacture, produce, or process tangible personal property. A manufacturer's taxable purchases include machines, tools, furniture, forklifts, generators, and office equipment.

However, existing law[2] contains a specific sales and use tax exclusion for tangible personal property purchased by "participating parties" for certain approved manufacturing "projects." Under the law,[3] the CAEATFA is authorized to approve sales and use tax exclusions for tangible personal property utilized for the design, manufacture, production, or assembly of, advanced transportation technologies or alternative source products, components, or systems, which includes renewable energy equipment, combined heat and power equipment, alternative transportation equipment, and advanced manufacturing projects. The law does not require that the tangible personal property be purchased or utilized in this state for purposes of the sales and use tax exclusion.

Under the law,[4] a "participating party" means a person, federal or state agency, department, board, authority, or commission, state or community college, or university, or a city or county, regional agency, public district, school district, or other political entity *engaged in business or operations in the state*, whether organized for profit or not for profit, that applies for financial assistance from CAEATFA for the purpose of implementing a project.

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[1] Part 1, Division 2 (commencing with Section 6001) of the Revenue and Taxation Code (RTC).
[2] RTC Section 6010.8.
[3] Public Resources Code (PRC) Section 26011.8.
[4] PRC Section 26003(a)(7).

Participating parties apply to the CAEATFA to receive the sales and use tax exclusion. For approval of qualifying projects, the law[5] requires the CAEATFA to consider a variety of factors related to whether the project results in a net benefit to the State, with consideration to both fiscal and environmental benefits.

The law[6] provides a $100 million cap for these sales and use tax exclusions.

California's sales and use tax rates. Effective January 1, 2013, a statewide 7.5% sales and use tax rate applies to tangible personal property sales and purchases. The following table 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 (Revenue and Taxation Code (RTC) Sections 6051, 6051.3, 6201, and 6201.3)
1.0625%	Local Revenue Fund 2011	Realignment of local public safety services (RTC Sections 6051.15 and 6201.15)
0.25%	State (Fiscal Recovery Fund)	Repayment of the Economic Recovery Bonds (RTC Sections 6051.5 and 6201.5)
0.25%	State (Education Protection Account)	Until 01/01/17, schools and community college funding (Section 36, 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)
0.50%	State (Local Public Safety Fund)	Local governments to fund public safety services (Section 35, Article XIII, State Constitution)
1.00%	Local (City/County) 0.75% City and County 0.25% County	City and county general operations (RTC Section 7203.1, operative 7/1/04); Dedicated to county transportation purposes
7.50%	Total Statewide Rate	

AMENDMENT

This bill clarifies the definition of "participating party" for purposes of the sales and use tax exclusions approved by CAEATFA. It specifies that an entity located outside of the state, including an entity located overseas, is a participating party eligible to apply for financial assistance in the form of the sales and use tax exclusion if the participating party commits to, and demonstrates that, the party will be opening a manufacturing facility in the state.

The bill also redefines the term "project" for purposes of the sales and use tax exclusion to specify that the qualifying tangible personal property must be utilized in this state.

In addition, the bill states Legislative intent that this change clarifies existing law and ensures that an out-of-state entity or overseas entity is eligible to apply for financial assistance.

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[5] PRC Section 26011.8(d).
[6] PRC Section 26011.8(h).

Also, the bill deletes a required report to the Legislature by the Governor's Office of Business and Economic Development related to jobs in advanced manufacturing, and makes other technical, nonsubstantive changes.

COMMENTS

1. **Purpose.** This bill intends to clarify that "participating party" includes out-of-state or overseas entities committed to opening a manufacturing facility in California. According to the author's office, recent legislation that expanded CAEATFA's authority to approve sales and use tax exclusions was enacted to promote the creation of California-based manufacturing, California-based jobs, the reduction of greenhouse gases, or reductions in air and water pollution or energy consumption. The author's office notes that CAEATFA's exclusion authority in law was not intended to exclude otherwise qualifying out-of-state and overseas entities desiring to open a manufacturing facility in California, and this bill makes that clear.
2. **Any change to the PRC's definition of "project" or "participating party" can have a direct sales and use tax implication.** The exclusion provided in the RTC is linked directly with the term "project" and "participating party" as defined in the PRC. When either definition is changed within the context of the PRC, it can result in a direct state and local sales and use tax revenue impact. However, the law caps the allowable sales and use tax exclusions to $100 million annually.
3. **CAEATFA is the exclusion's primary administrator.** Consequently, the bill's enactment will have a minimal effect on the BOE's administrative duties.

Senate Bill 78 (Committee on Budget and Fiscal Review) Chapter 33

Medi-Cal Managed Care Plan Taxes

Urgency measure, effective June 27, 2013, but operative date depends on federal government approval. Among its provisions, adds and repeals Article 5 (commencing with Section 6174) of Chapter 2 of Part 1 of Division 2 of the Revenue and Taxation Code.

BILL SUMMARY

Among other things, this 2013-14 budget trailer bill does all of the following:

- Contingent upon specified federal participation and approval, imposes a 3.9375% sales tax on gross receipts derived from Medi-Cal managed care plans sold at retail in this state on and after July 1, 2013 to July 1, 2016, and
- Extends the insurance gross premiums tax on Medi-Cal managed care plans, from July 1, 2012, to July 1, 2013.

Sponsor: Committee on Budget & Fiscal Review

LAW PRIOR TO AMENDMENT

Sales Tax. Except where the law provides a specific exemption or exclusion, California's Sales and Use Tax Law[1] 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.

California's sales and use tax rates. Effective January 1, 2013, California imposes a statewide 7.5% sales and use tax on tangible personal property sales and purchases. 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 (Revenue and Taxation Code (RTC) Sections 6051, 6051.3, 6201, and 6201.3)
1.0625%	Local Revenue Fund 2011	Realignment of local public safety services (RTC Sections 6051.15 and 6201.15)
0.25%	State (Fiscal Recovery Fund)	Repayment of the Economic Recovery Bonds (RTC Sections 6051.5 and 6201.5)
0.25%	State (Education Protection Account)	Schools and community college funding (Section 36, 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)
0.50%	State (Local Public Safety Fund)	Local governments to fund public safety services (Section 35, Article XIII, State Constitution)

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

Rate	Jurisdiction	Purpose/Authority
1.00%	Local (City/County) 0.75% City and County 0.25% County	City and county general operations (RTC Section 7203.1, operative 7/1/04); Dedicated to county transportation purposes
7.50%	Total Statewide Rate	

Insurance Tax. The California Constitution[2] imposes a 2.35% tax on insurers doing business in California. Commonly referred to as the "gross premiums tax," the annual insurance tax is based on insurers' gross premiums, less return premiums. The California Constitution specifies that the 2.35% tax is in lieu of all other taxes and licenses, with specified exceptions. Any person that meets this constitutional provision's "insurer" definition must register with the Department of Insurance (DOI) and remit the annual gross premiums tax.

Medi-Cal Managed Care Plans. As defined in the Constitution, "insurer" does not expressly include a health care service plan, such as a Medi-Cal managed care plan. The Knox-Keene Health Care Service Plan Act covers these providers. Therefore, these plans are not generally prohibited from other taxation.

Existing law[3] defines a "Medi-Cal managed care plan" to mean any individual, organization, or entity, other than an insurer or a dental managed care plan, that enters into a specified contract with the State Department of Health Care Services (DHCS), as described.

The "in lieu of" provision that currently exempts insurers from all other state and local taxes and licenses (with certain specified exceptions) does not apply to a Medi-Cal managed care plan. Accordingly, Medi-Cal managed care plans continue to be subject to other state, county, and municipal taxes and licenses, as applicable.

Until July 1, 2012, existing law[4] imposes a 2.35% annual tax on every Medi-Cal managed care plan doing business in this state. The tax revenues are remitted to the DOI, and are continuously appropriated to the DHCS for the Medi-Cal program in an amount equal to the difference between 100% and the applicable federal medical assistance percentage, with the balance appropriated to the Managed Risk Medical Insurance Board for purposes of the Healthy Families Program.

This Medi-Cal managed care plan tax is imposed on the "total operating revenues," which means all premium or capitation payments a Medi-Cal managed care plan receives for health care services, including, but not limited to, Medi-Cal services. Total operating revenues do not include amounts Medi-Cal managed care plans receive pursuant to a subcontract with a Medi-Cal managed care plan to provide Medi-Cal beneficiaries health care services.

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[2] Article XIII, Section 28.
[3] RTC Section 12009.
[4] RTC Section 12201.

AMENDMENT

Among other things, this bill adds RTC Article 5 (commencing with Section 6174) to do the following:

- From July 1, 2013 until July 1, 2016, impose a 3.9375% sales tax on sellers of Medi-Cal health care services at retail, measured by the gross receipts from the sale of those services.
- For efficient administration of the tax, require sellers that are actively engaged in the retail sale of Medi-Cal health care services to register, report, and pay the tax to the BOE.
- Specify that sales tax prepayments shall not apply to sellers until no later than three months after the date that federal financial participation is available and any necessary federal approvals are obtained.
- Define "seller" to mean any person, other than specified insurers and dental managed care plans, or any entity that enters into a contract with the DHCS pursuant to specified provisions.
- Define "gross receipts" to mean the total premium or capitation payments Medi-Cal managed care plan sellers receive for health care services coverage or provision, including, but not limited to, Medi-Cal services. Excludes amounts received pursuant to a subcontract with a Medi-Cal managed care plan to provide health care services to Medi-Cal beneficiaries.
- Require the proposed tax revenues to be deposited in the State Treasury to the credit of the Children's Health and Human Services Special Fund.
- Prohibits counties, cities and districts from imposing a sales or use tax on the gross receipts described in the bill.
- Specifies that this article shall be implemented only if and to the extent that federal financial participation under specified federal law is available and any necessary federal approvals have been obtained. This article is automatically repealed if it is delayed based upon a challenge under federal law.
- Specifies that this article shall have no force or effect if there is a final judicial determination made by any state or federal court that is not appealed, in any action by any party, or a final determination by the administrator of the federal Centers for Medicare and Medicaid Services, that disallows, defers, or alters the implementation of this article.

The bill also makes numerous changes to the Tax on Insurers Law[5] to restore the 2.35% gross premiums tax on every Medi-Cal managed care plan in this state, from July 1, 2012 to July 1, 2013.

As an urgency bill, these provisions take effect immediately, but the imposition of the sales tax is contingent upon specified federal participation and approval.

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[5] Part 7, Division 2 (commencing with Section 12201) of the RTC.

IN GENERAL

Medi-Cal is California's Medicaid program. The DHCS's website describes Medi-Cal as a public health insurance program which provides needed health care services for low-income individuals including families with children, seniors, persons with disabilities, foster care, pregnant women, and low income people with specific diseases such as tuberculosis, breast cancer, or HIV/AIDS. The state and federal government finance Medi-Cal equally .

BACKGROUND

In 2009, Assembly Bill 1422[6] subjected the Medi-Cal managed care plans' total operating revenues to the 2.35% insurance gross premiums tax, until December 31, 2010. In 2010, Assembly Bill 853[7] extended the gross premiums tax on Medi-Cal managed care plans to July 1, 2011. Subsequently, Assembly Bill x1 21[8] extended the sunset date to July 1, 2012. This Medi-Cal managed care plan tax expired July 1, 2012.

COMMENTS

1. **Purpose.** Among other things, this 2013-14 Budget trailer bill intends to increase tax revenues to draw down federal Medi-Cal funds. These federal Medi-Cal funds will be used to pay back Medi-Cal managed care plan providers and to offset General Fund expenditures for Medi-Cal managed care rates for children, seniors, the disabled, and other eligible persons.

2. **The State pays for the plans.** According to the Department of Finance, 24 managed health care plan providers will be subject to the proposed tax, and the State, rather than the beneficiaries, will pay the premiums for these plans. These 24 providers, who had been remitting the gross premiums tax to the DOI, will now be required to remit the 3.9375% sales tax to the BOE.

3. **Bill requires providers to report their tax obligations three times more frequently.** Currently, if the *annual* tax liability is $5,000 or more, Medi-Cal managed care plan providers are required to make quarterly prepayments to the DOI on or before April 1, June 1, September 1, and December 1.

   This bill requires these providers to file returns quarterly, generally by April 30, July 31, October 31, and December 31. However, if their taxable gross receipts average $17,000 or more per month (equal to a *monthly* tax liability of $4,794 or more, or $57,528 in tax annually[9]), the providers must, in addition to the quarterly returns, make two prepayments within each quarter.

4. **What if federal approvals occur after return or prepayment due dates?** The tax becomes operative on July 1, 2013. However, the bill specifies that the provisions shall be implemented only if and to the extent federal financial participation and approvals have occurred. If federal participation and approvals occur *after* the first tax reporting date, will sellers be subject to delinquency charges if they have not remitted the tax? Current law automatically imposes a 10% penalty on the late payment (6% for late prepayments) and 6% interest annually. Although penalty relief is available,

[6] Ch. 157, Stats. 2009.
[7] Ch. 717 Stats. 2010.
[8] Ch. 11 Stats. 2011.
[9] $17,000 x 12 months x 2.35% = $4,794 per month x 12 months = $57,924.

the law[10] requires sellers seeking relief to file a statement under penalty of perjury setting forth the grounds for relief.

5. **Bill doesn't provide the BOE or affected sellers with much lead time.** Although the bill specifies that sales tax prepayments shall not apply to sellers "until no later than three months" after the date federal approval is obtained, the tax is implemented the date the federal approval is made. This provides virtually no time to enable the BOE to provide affected sellers with tax reporting and remittance instructions.

6. **The bill's language is patterned after a similar in-home support services (IHSS) sales tax.** In 2009, legislation[11] was enacted to impose a sales tax on IHSS providers, measured by the providers' gross receipts from their services. Similar to this bill, this tax will only become operative if specified federal approval requests for matching funds are granted. To date, federal approval has not occurred, and the BOE has not yet implemented the tax.

7. **The BOE staff does not foresee any administrative problems with the gross premiums tax one-year extension.** The BOE, the DOI, and the Controller all contribute to insurance tax administration. The Controller acts as a collector of any delinquent tax. The DOI primarily licenses, regulates, and audits insurers, and assesses and collects the tax amount each insurer is required to pay. The BOE issues DOI-determined assessments, makes refunds, and evaluates appeals.

   This one-year 2.35% Medi-Cal managed care plan tax extension will not change the BOE's responsibilities.

[10] RTC Section 6592.
[11] AB 1612 (Ch. 725, Stats. 2009, Committee on Budget).

Senate Bill 90 (Galgiani) Chapter 70

Manufacturing and Research and Development Exemption

Urgency measure, effective July 11, 2013, but operative July 1, 2014. Among its provisions, amends Section 6377.1 of the Revenue and Taxation Code.

BILL SUMMARY

Among other things, beginning July 1, 2014, and until July 1, 2022, this bill provides manufacturers, biotechnology and other physical, engineering, and life science researchers and developers a 4.1875% sales and use tax exemption for their purchases of qualifying tangible personal property.

Sponsor: Senators Galgiani and Cannella

LAW PRIOR TO AMENDMENT

Except where the law provides a specific exemption or exclusion, California's Sales and Use Tax Law[1] 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.

Generally, sales or use tax applies to the sale or purchase of tangible personal property to persons who use the property to manufacture, produce or process tangible personal property. A manufacturer's taxable purchases include machines, tools, furniture, forklifts, generators, and office equipment. A software publisher's taxable purchases include computer equipment, such as servers, routers, switches, power units, network devices, hard drives, processors, memory modules, and other computer hardware and components. An electric power generating facility's taxable purchases include transformers, alternators, generators, transmitters, turbines and solar panels. A biotechnology researcher's taxable purchases include various lab tools, workstations, monitors, and analyzers.

Conversely, tax does not apply to sales of tangible personal property when the purchasers physically incorporate that property into the manufactured article to be sold. For example, no tax applies to a manufacturer's raw material purchases when, prior to making a taxable use, they become an ingredient or component part of the manufactured article to be resold.

California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA). Existing law[2] contains a specific sales and use tax exclusion[3] for tangible personal property purchased for certain approved manufacturing projects. In 2010, legislation[4] authorized the CAEATFA to approve sales and use tax exclusions for tangible personal property utilized for the design, manufacture, production, or assembly of

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[1] Part 1 of Division 2 (commencing with Section 6001) of the Revenue and Taxation Code (RTC).
[2] RTC Section 6010.8.
[3] An "exclusion" means the transfer of the property is neither a "sale" nor a "purchase" and is therefore excluded from the application of the sales and use tax. An "exemption" involves a retail sale that, absent an exemption in law, would otherwise be subject to the tax.
[4] SB 71 (Ch. 10, Stats. 2010, effective March 24, 2010).

advanced transportation technologies or alternative energy source products, components or systems. In 2012, legislation[5] was enacted to authorize CAEATFA to approve sales and use tax exclusions related to advanced manufacturing projects until July 1, 2016. The law[6] provides a $100 million cap for these exclusions.

CAEATFA's approval of these exclusions is based on whether the project results in a net benefit to the State, with consideration to both fiscal and environmental benefits.

California's sales and use tax rates. Effective January 1, 2013, California imposes a statewide 7.5% sales and use tax on tangible personal property sales and purchases. 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 (Revenue and Taxation Code (RTC) Sections 6051, 6051.3, 6201, and 6201.3)
1.0625%	Local Revenue Fund 2011	Realignment of local public safety services (RTC Sections 6051.15 and 6201.15)
0.25%	State (Fiscal Recovery Fund)	Repayment of the Economic Recovery Bonds (RTC Sections 6051.5 and 6201.5)
0.25%	State (Education Protection Account)	Schools and community college funding (Section 36, Article XIII, State Constitution) (until 01/01/17)
0.50%	State (Local Revenue Fund)	Local governments to fund health and welfare programs (RTC Sections 6051.2 and 6201.2)
0.50%	State (Local Public Safety Fund)	Local governments to fund public safety services (Section 35, Article XIII, State Constitution)
1.00%	Local (City/County) 0.75% City and County 0.25% County	City and county general operations (RTC Section 7203.1, operative 7/1/04); Dedicated to county transportation purposes
7.50%	Total Statewide Rate	

AMENDMENT

Beginning July 1, 2014, and until July 1, 2022, this bill provides a 4.1875% sales and use tax exemption for a "qualified person's" purchases of:

- Qualified tangible personal property to be used primarily in manufacturing, processing, refining, fabricating, or recycling of property (i.e., machinery, equipment, parts, belts, shafts, computers, software, pollution control equipment, buildings and foundations), as specified.
- Qualified tangible personal property to be used primarily to maintain, repair, measure, or test any qualified tangible personal property.
- Qualified tangible personal property purchased by a contractor, as specified, for use in the performance of a qualified person's construction contract. The qualified person

[5] SB 1128 (Ch. 677, Stats. 2011, effective January 1, 2013).
[6] Public Resources Code Section 26011.8.

must use the property, however, as an integral part of any manufacturing, processing, refining, fabricating, or recycling process or as a research or storage facility in connection with the manufacturing process.

- Qualified tangible personal property to be used primarily in research and development (R&D).

The bill excludes from the "qualified person" definition an apportioning trade or business that is required to apportion its business income pursuant to specified provisions. This includes business activity relating to the production, refining, or processing of oil, natural gas, or mineral ore.

The bill also limits the allowable exemption to $200 million in qualifying purchases each calendar year by each qualified person or by all qualified persons required or authorized to be included in a combined report under the Corporation Tax Law.[7]

The bill defines "fabricating," "manufacturing," "primarily," "process," "processing," "refining," "research and development," and "useful life." The bill also specifies the tangible personal property included or excluded from the proposed partial exemption.

The proposed partial exemption excludes:

- Consumables with less than a one year useful life,
- Furniture, inventory, equipment used in the extraction process or equipment used to store finished products that have completed the manufacturing process, and
- Tangible personal property primarily used in administration, general management, or marketing.

The bill excludes from the exemption, any city, county, or district tax levied pursuant to the Bradley-Burns Uniform Local Sales and Use Tax Law or the Transactions and Use Tax Law. It also excludes the 1.0625% Local Revenue Fund 2011, 0.5% Local Revenue Fund, the 0.5% Local Public Safety Fund, and the 0.25% Fiscal Recovery Fund components. The proposed exemption includes the two remaining state sales and use tax components.[8]

The bill contains additional provisions outside the BOE's purview, which are not discussed in this analysis.

BACKGROUND

For a ten-year period ending December 31, 2003, the law provided new manufacturers with a state General Fund sales and use tax exemption on their purchases of specified manufacturing equipment. Also, the law provided manufacturers income and corporation tax credits (MIC) of 6% for similar equipment placed in service in California. Similar to the exemption proposed in this bill, the partial exemption and credit related to equipment used primarily for manufacturing, refining, processing, fabricating or recycling. New manufacturers could claim the partial exemption or the MIC. However, existing manufacturers could only claim the MIC.

[7] Revenue and Taxation Code Section 25101 or 25101.15.
[8] 3.9375% General Fund, 0.25% Education Protection Account.

This partial exemption and MIC contained a conditional sunset date. The law required these provisions to sunset when manufacturing employment,[9] less aerospace employment, failed to exceed January 1, 1994 manufacturing employment by more than 100,000. On January 1, 2003, the employment figures were less than the 1994 number by over 10,000. Therefore, the partial exemption and MIC sunset at the end of 2003.

Legislative History. Since then, numerous bills have been introduced to reinstate, expand, or modify the exemption and/or MIC, but all failed to pass. Bills introduced during the last two Legislative sessions that exempted similar purchases from sales and use tax include:

Bill No.	Session	Author	Proposed Exemption
ABx1 40	2011-12	Allen	3.9375% exemption for new businesses and 3% for existing businesses engaged in manufacturing, software production, biotechnology research and development, and renewable power generation facilities.
AB 103	2011-12	Budget committee	5% exemption for new manufacturers and software producers, and 1% for existing manufacturers and software producers.
AB 218	2011-12	Wieckowski	5.25% exemption for manufacturers and software producers.
AB 303	2011-12	Knight	5% exemption for new manufacturers.
AB 979	2011-12	Silva	5% exemption for manufacturers and software producers and affiliates.
AB 1057	2011-12	Olsen	5% exemption for manufacturing, research and development, and air pollution mitigation by manufacturers and affiliates.
SB 116	2011-12	Dutton	Same as ABx1 40 above.
SB 395	2011-12	Dutton	5% exemption for manufacturing and software production.
AB 1911	2011-12	Donnelly	3.9375% exemption for manufacturing and software production.
AB 1972	2011-12	Huber	Full exemption for manufacturing, software production, biotechnology research and development, and renewable power generation facilities.
SB 686	2011-12	Padilla	Full exemption for biotechnology manufacturing and research and development activities.
AB 810 and AB 829	2009-10	Caballero	5% exemption for qualifying tangible personal property, and 6% exemption for sustainable development equipment investments by manufacturing and software production.
AB 1719	2009-10	Harkey	6% exemption for manufacturing.
AB 1812	2009-10	Silva	6% exemption for manufacturing and software production.
AB 2280	2009-10	Miller	Full exemption for manufacturing.
SB 1053	2009-10	Runner	6% exemption for manufacturing and software publishing and their affiliates.

[9] As determined by the Employment Development Department.

Bill No.	Session	Author	Proposed Exemption
SBx6 18	2009-10	Steinberg & Alquist	6% exemption for specific manufacturing and software production activities.
SBx6 8 & SBx6 44	2009-10	Dutton	6% exemption for manufacturers and software publishers and affiliates.

COMMENTS

1. **Purpose.** This is part of Governor Brown's 2013-14 Budget revision plan to revamp the state's enterprise zone and hiring credit programs to encourage manufacturing investment and increase employment in high-poverty areas. This bill supersedes AB 93, also part of Governor Brown's 2013-14 Budget revision measure.

2. **The bill references various NAICS codes to describe qualifying taxpayers.**

   NAICS codes 3111 to 3399 include all establishments primarily engaged in manufacturing activities. This includes manufacturers in the aerospace sector, textiles, pharmaceuticals, printing, food, and more.

   NAICS code 541711 includes establishments primarily engaged in conducting biotechnology research and experimental development. This involves the study of the use of microorganisms and cellular and biomolecular processes to develop or alter living or non-living materials. This biotechnology R&D may result in new biotechnology processes or in new or genetically-altered product prototypes that various industries may reproduce or utilize.

   NAICS code 541712 includes establishments primarily engaged in conducting research and experimental development (except biotechnology research and related experimental development) in the physical, engineering, and life sciences, such as agriculture, electronics, environmental, biology, botany, computers, chemistry, food, fisheries, forests, geology, health, mathematics, medicine, oceanography, pharmacy, physics, veterinary and other allied subjects.

3. **Partial exemptions complicate administration of the tax.** Currently, most sales and use tax exemptions apply to the total applicable sales and use tax. However, California law contains a partial exemption for sales of gas (at a 5.25% rate) and five partial exemptions at a 5.5%[10] rate, as follows:

   (1) Farm equipment and machinery,

   (2) Diesel fuel used for farming and food processing,

   (3) Teleproduction and postproduction equipment,

   (4) Timber harvesting equipment and machinery, and

   (5) Racehorse breeding stock.

   These partial tax exemptions complicate retailers' return preparation and return processing. Return errors occur frequently with claimed partial exemptions. Accordingly, the BOE's return processing workload increases.

[10] 3.9375% General Fund, 1.0625% Local Revenue Fund 2011, 0.25% Fiscal Recovery Fund, and 0.25% Education Protection Account.

Also, this bill proposes a new 4.1875% exemption rate. This requires a sales and use tax return revision with a new, separate return computation. If enacted, some retailers may be required to segregate the 4.1875% exempt sales, the 5.50% exempt sales, fully exempted sales (e.g., a resale sale or interstate commerce sale), and fully taxable sales. This adds a new level of complexity, and potentially increases tax reporting errors. Accordingly, the BOE's tax administrative functions and retailers' reporting obligations become more complicated.

Senate Bill 442 (Wyland) Chapter 253

Taxpayers' Rights: BOE Collection Errors

Effective January 1, 2014. Among its provisions, amends Section 7096 of the Revenue and Taxation Code.

BILL SUMMARY

For purposes of the Sales and Use Tax Law, this bill changes the trigger of the 90-day deadline for filing a reimbursement claim from the date of the BOE's erroneous action to the date the taxpayer incurred the bank and third-party charges.

Sponsor: Board of Equalization

LAW PRIOR TO AMENDMENT

Current law authorizes the BOE to seize property of a delinquent taxpayer. Existing law also authorizes the BOE to issue a levy or notice to withhold to satisfy tax obligations of a delinquent taxpayer.

Revenue and Taxation Code (RTC) Section 7096 allows a taxpayer to file a reimbursement claim with the BOE for bank charges and any other reasonable third-party check charge fees (charges and fees). The charges and fees must directly result from an erroneous levy or notice to withhold, erroneous processing action, or erroneous collection action. A taxpayer is required to file a claim within 90 days from the date of BOE's erroneous action, and the BOE must respond within 30 days from the date the claim is received.

AMENDMENT

This bill authorizes a taxpayer to file the reimbursement claim within 90 days from the date the taxpayer incurs the bank and third-party charges.

COMMENTS

1. **Purpose.** This bill is intended to provide taxpayers with relief from charges and fees incurred due to an erroneous BOE collection or processing action.
2. **Stringent filing deadline.** Sometimes taxpayers are unable to file a claim within 90 days from the erroneous BOE action date.

   In one example, the BOE filed an erroneous levy and sent the taxpayer's Notice of Levy to an incorrect address. Additionally, the taxpayer's financial institution delayed compliance with the levy for nearly three months. As a result, the financial institution sent the first levy notice to the taxpayer about three months from the erroneous BOE action date. The erroneous levy resulted in early withdrawal fees and bank processing fees. The taxpayer failed to meet the 90-day reimbursement claim deadline due to the delayed levy notice. Existing law required the BOE to deny the claim even though the taxpayer met all other conditions.

   This bill revises the basis of the 90-day reimbursement claim filing deadline from the erroneous BOE action date to the date the taxpayer incurs the bank and third-party charges. This change provides a dependable measure to ensure a taxpayer receives at least one of the two action notices: either the BOE notice, or the bank or third-party notice of action. Had this timetable been in law for the previously cited taxpayer, the taxpayer would have met the reimbursement claim deadline since the 90-day clock would not have started ticking until the bank levied the taxpayer's account.

Senate Bill 788 (Committee on Transportation and Housing) Chapter 523

Prepaid Sales Tax on Jet Fuel: Calculation

Effective January 1, 2014. Among its provisions, amends Section 6480.1 of the Revenue and Taxation Code.

BILL SUMMARY

Among its provisions, this bill:

- Amends the sale prepayment provision[1] to make the aircraft jet fuel and diesel fuel statutory language consistent with the language for motor vehicle fuel (gasoline), and
- Contains a technical correction to align rate setting dates for the jet fuel sales tax prepayment rate.

Sponsor: Committee on Transportation and Housing

LAW PRIOR TO AMENDMENT

Existing law[2] requires a supplier of gasoline, diesel fuel, or aircraft jet fuel to collect a sales tax prepayment from the retailer that buys the fuel. By March 1 of the same year, the BOE determines and sets the effective date of the sales tax prepayment rates. BOE notifies every supplier, wholesaler, and retailer of gasoline, diesel fuel, and aircraft jet fuel by May 1. The adjusted prepayment rates are effective for the following July 1 through June 30.

The per-gallon gasoline, aircraft jet fuel and diesel fuel prepayment rate is based upon 80% of the combined state and local sales tax rate on the average selling price of the fuel, excluding sales tax, as determined by industry publications. The BOE currently uses the sales price data reported by the United States Energy Information Administration, a petroleum and fuel industry publication.

In 2010, two “fuel tax swap” measures[3] changed the imposition and rates of state taxes on gasoline and diesel fuel, and required the BOE to determine the appropriate excise tax rate adjustments to maintain revenue neutrality. The gasoline tax changes became operative on July 1, 2010, and the diesel fuel tax changes became operative on July 1, 2011.

The fuel tax swap provisions require the BOE to maintain revenue neutrality, so that the revenues derived from the increased gasoline excise tax and the increased diesel sales and use tax equals the revenues that would have been derived had the gasoline sales and use tax partial exemption and the diesel fuel excise tax reduction, respectively, not occurred.

The BOE determines the excise tax rate adjustments by March 1 of each year, and the adjusted rate applies on the following July 1.

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[1] Revenue and Taxation Code (RTC) Section 6480.1.
[2] RTC Section 6480.1.
[3] ABx8 6, (Ch. 11, Stats. 2010) and SB 70 (Ch. 9, Stats. 2010). These provisions were reenacted in 2011 by AB 105 (Ch. 6, Stats 2011).

AMENDMENT

This bill clarifies that the average sales price of aircraft jet fuel and diesel fuel is based on published industry reports that are used to compute the sales tax prepayment rate for those fuels. This change conforms the references to that used for gasoline.

This bill also makes a technical change in order to correct a drafting error.

BACKGROUND

Last year, the BOE sponsored legislation[4] that aligned the sales tax prepayment dates with the fuel tax swap excise tax rate adjustment dates. Two words in the jet fuel sales tax prepayment language were inconsistent with the changes made to both the gasoline and diesel fuel provisions.

Additionally, last year's bill deleted a reference to a specified publication, the "Quarterly Oil Report," as reported by the State Energy Resources Conservation and Development Commission. That report is no longer published or used by the BOE to obtain the selling price of the respective fuels. The BOE currently uses the data reported by the United States Energy Information Administration, a petroleum and fuel industry publication.

COMMENTS

1. **Purpose.** This bill contains multiple, non-controversial changes to statutes so that the Legislature can make minor amendments in a cost-effective manner. The amendment to RTC Section 6480.1 is one such provision.
2. **BOE staff has no administrative concerns.** This bill makes two minor changes to the sales tax prepayment of fuels provisions. One is a minor clean-up to last year's BOE-sponsored bill, which ensures the rate setting is done in March of the **same year** that the rate change takes effect. The other is a revision that simplifies the aircraft jet fuel and diesel fuel statutory language and makes it consistent with the language for gasoline.

[4] AB 2679 (Ch. 769, Stats. 2012), effective January 1, 2013.

TABLE OF SECTIONS AFFECTED

SECTIONS		BILL AND CHAPTER NUMBER		SUBJECT
Revenue & Taxation Code				
§97.68	Amend	AB 92	Ch. 26	Triple flip sunset
Article 5 (§6174)	Add Repeal	SB 78	Ch. 33	Sales tax on Medi-cal managed care plans
§6363.4	Amend	AB 163	Ch. 72	Military thrift stores exemption
§6377.1	Amend	SB 90	Ch. 70	Manufacturing exemption
§6412	Add Repeal	AB 143	Ch. 687	Military transfers: use tax exemption
§6480.1	Amend	SB 788	Ch. 523	Prepayments: aircraft jet fuel
§7096	Amend	SB 442	Ch. 253	Taxpayers' rights: reimbursement claim filing deadline
§7153.6	Add	AB 781	Ch. 532	Sales suppression device prohibition
§7291	Amend	AB 210	Ch. 194	Authorization to levy; counties of alameda and contra costa
§7292	Amend	AB 210	Ch. 194	Operative date: counties of alameda and contra costa
Government Code				
Part 12.2 (§15910)	Add Repeal	AB 576	Ch. 614	Revenue Recovery and Collaborative Enforcement Team Act
Public Resources Code				
§26003	Amend	AB 1422	Ch. 540	California Alternative Energy and Advanced Transportation Financing Authority exclusion: participating party