

[Senate Bill 480](#) (Pan)

Date: 02/26/15

Program: Heavy Equipment Rental Tax

Sponsor: American Rental Association

Revenue and Taxation Code Sections 97.38 and Part 11 (commencing with Section 5500)

Effective: January 1, 2016

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Summary: In lieu of business personal property tax, imposes a 0.75% tax on a renter of qualified heavy equipment and requires the Board of Equalization (BOE) to administer the proposed tax.

Purpose: To address unfair and inconsistent taxation of heavy equipment. Specifically, rental companies with multiple locations in the state are subjected to numerous audits each year in different jurisdictions. They contend that different county assessors use different methods for valuing mobile construction equipment.

Fiscal Impact Summary: Annual revenue increase of \$21 million in heavy equipment rental tax and \$1.8 million in state and local sales tax.

Existing Law: Property Tax. Under existing law,¹ all property is taxable unless specifically exempt under the Constitution or Revenue and Taxation Code. The county assessor determines taxability each year, generally on the January 1 lien date.

Personal property used in a trade or business is generally taxable. Property owners must file an annual business property statement with the county assessor to report the property's cost.² The assessor values the personal property each lien date at its current fair market value. Generally, the assessor determines the current fair market value based on the property's acquisition cost with adjustments for inflation and depreciation.

The personal property tax rate is the same as the rate levied on real property. That rate is 1%, plus any local voter-approved indebtedness.

Regarding personal property taxation, California's Constitution³ authorizes the Legislature by a 2/3 vote to classify personal property for different taxation or for exemption.

The law provides no specific tax exemption for heavy equipment leases or rentals (rentals). However, a personal property business inventory exemption⁴ is available. Personal property intended for rent in the regular course of business that is *not* rented on the January 1 lien date is exempt from taxation for the upcoming fiscal year (July 1 to June 30). That property is regarded as business inventory on that particular day, even if the property is rented in the regular course of business for the other 364 days of the year.

Revenue Distribution. Generally, personal property tax revenues are allocated according to the property's "situs" (location) and accrue only to those taxing jurisdictions in the tax rate area where the property is located. Under a Board of Equalization (BOE) rule,⁵ property rented on a daily, weekly, or other short-term basis (six months or less) has situs where the property's owner (the renter) normally keeps the property. Temporary absences from that location do not change the property's situs. For property rented for an extended, but unspecified, period or more than a 6-month term, the assessor determines the property's situs based on the rentee's use. For typical equipment rentals, generally the

¹ Part 1 (commencing with Section 50) of Division 1 of the Revenue and Taxation Code (RTC).

² RTC Section 441.

³ California Constitution Article XIII, Section 2.

⁴ RTC Section 219.

⁵ Property Tax Rule 204.

equipment's owner is the assessee subject to the tax.⁶ However, the facts specific to each case determine the assessee.

Proposed Law: Beginning July 1, 2016, this bill imposes⁷ a 0.75% tax on a renter, as defined, for a qualified heavy equipment rental, as defined. The proposed tax is in lieu of any property tax on this equipment. The bill requires the heavy equipment's qualified renter to collect the tax on the rental price, and requires the BOE to administer the tax.

The bill specifies that a business' qualified heavy equipment that is not for rent shall remain subject to any applicable property taxes.

The bill imposes requirements on the county auditor related to personal property tax adjustments.

Administration. This bill requires the BOE to administer and collect the tax pursuant to the Fee Collection Procedures Law (FCPL).⁸ The bill clarifies that under the FCPL:

- "Fee" includes the tax; and
- "Feepayer" includes a person that is liable for payment of the tax.

The FCPL provides the BOE with the general statutory framework to administer its various fee programs. Among other things, the FCPL provides for collection, reporting, return, refund, and appeals procedures, as well as the BOE's authority to adopt regulations related to the FCPL's administration and enforcement. The bill also specifically authorizes the BOE to prescribe and adopt tax administration and enforcement regulations.

Registration, Reporting, and Payment. The bill requires every qualified renter to register with the BOE using a BOE-prescribed application, as described.

The tax imposed is due and payable to the BOE quarterly on or before the last day of the month following each calendar quarter. Qualified renters must file a return using electronic media on or before the last day of the month following each quarterly period.

Both the application and the return may be authenticated in a form or pursuant to a method as the BOE may prescribe.

Disposition of Proceeds. This bill requires all revenues, interest, penalties, and other amounts collected, less refunds and the BOE's administrative costs, to be deposited in the state's General Fund.

Definitions. This bill defines several key terms, as follows:

- "**Qualified renter**" means a renter (1) whose principal business is qualified heavy equipment rentals, and (2) is engaged in a line of business described in the 2012 edition of the North American Industry Classification System (NAICS) Code 532412, as specified.
- "**Rental price**" means the total charge for renting the equipment, excluding other charges as specified.
- "**Renting**" or "**rent**" means a rental for a period of less than 365 days or for an undefined period, or an open-ended contract.
- "**Qualified heavy equipment**" means construction, earthmoving, or industrial equipment that is mobile, including, but not limited to the following:
 - (1) A self-propelled vehicle that is not designed to be driven on the highway.

⁶ RTC Section 405.

⁷ Part 11 (commencing with Section 5500).

⁸ RTC Part 30 (commencing with Section 55001).

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- (2) Industrial electrical generation equipment or portable heating, ventilating, and air-conditioning equipment.
- (3) Industrial lift equipment.
- (4) Industrial material equipment.
- (5) Equipment used in shoring, shielding, and ground trenching.
- (6) Equipment or vehicles not subject to the Vehicle License Fee.

Background: Last year's [AB 2114](#) (Pan) proposed a similar tax, and the Assembly Appropriations Committee held the bill. 2013's [AB 1055](#) (Pan) and 2012's [AB 1941](#) (Ma) also proposed a similar tax. The Assembly Revenue and Taxation Committee held both bills.

Commentary:

1. **Effect of the bill.** This bill changes the method of taxation for short-term rentals of heavy equipment by imposing a 0.75% tax on the rental price, rather than subjecting the equipment's value to personal property tax.
2. **For personal property tax, the Legislature has authority to change taxation method.** Heavy equipment, as described in the bill, is regarded as personal property upon which property tax is assessed. As personal property, the Legislature is constitutionally authorized to provide for a differential tax, such as the tax the bill proposes. The law provides a similar differential tax on vehicles. In 1936, the creation of the Vehicle License Fee removed vehicles from local county assessment and subjected them to a Department of Motor Vehicles-administered vehicle license fee. The fee is in lieu of the property tax under current law.⁹ The 1936 change stemmed from the inability to effectively assess and collect taxes on vehicles via the property tax. Noted problems at the time included significant tax evasion, relatively high administrative costs, and little statewide uniformity in values assigned to similar vehicles.
3. **Implementation Costs.** Although the bill authorizes reimbursement of the BOE's costs through the revenues collected, in order for the BOE to receive funding for the necessary implementation costs up front, it is recommended that the bill authorize the Director of Finance to authorize a loan from the General Fund to the BOE to meet cash needs.
4. **Who is a "qualified renter?"** The bill defines a qualified renter as one whose principal business is the short-term rental of qualified heavy equipment and who is engaged in a business described in NAICS Industry Code 532412. This code describes establishments that are primarily engaged in a line of business renting or leasing heavy equipment without operators that may be used for construction, mining, or forestry. This includes bulldozers, earthmoving equipment, oil well or other well-drilling machinery and equipment, logging, or cranes.
5. **What about bad debts?** The author may wish to consider adding a provision that relieves a qualified renter from the tax liability for accounts found worthless and charged-off for income tax purposes.
6. **The renters' receipts from the proposed rental tax will be subject to California's use tax.** Under California's Sales and Use Tax Law,¹⁰ "sales price"¹¹ means the total amount for which tangible personal property is sold or leased or rented. In the case of a taxable lease, generally, if a lessor does not elect to pay tax when purchasing the property, use tax measured by the rentals payable is imposed on the lessee and must be collected by the lessor upon payment.¹² "Rentals Payable"

⁹ RTC Section 10758.

¹⁰ Part 1 of Division 2 (commencing with Section 6001) of the Revenue and Taxation Code (RTC).

¹¹ RTC Section 6011.

¹² Regulation 1660(c).

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includes, subject to certain exceptions, any payments required by the lease, including personal property taxes, whether assessed directly against the lessee or against the lessor. The bill imposes the heavy equipment tax on the renter. Therefore, if the renter (lessor) passes the cost of the tax on to the customer (lessee), the tax is part of the rentals payable by which the use tax is measured.

Administrative Costs: BOE administrative costs related to this bill are likely to be significant. These costs include taxpayer identification, notification, and registration; regulation development; manual and publication revisions; tax return design; computer programming; return, payment, and refund claim processing; audit and collection tasks; staff training; and public inquiry responses. A detailed cost estimate is pending.

Revenue Impact:

Background, Methodology and Assumptions:

Heavy equipment rental receipts: According to the 2012 United States (U.S) Economic Census, 2012 NAICS code 532412 receipts amounted to \$19.4 billion. At the time staff prepared this estimate, 2012 California receipt data was unavailable. Based on 2007 Census data, staff estimates that California's share of the U.S. receipts is 11%. Accordingly, 2012 estimated California NAICS code 532412 rental receipts amount to \$2.1 billion ($11\% \times \$19.4 \text{ billion} = \2.1 billion).

NAICS code 532412's, "Products Line Statistics by Industry" indicates that these receipts include rentals other than qualified heavy equipment rentals described in the bill, such as social events equipment and office furniture rentals. Staff estimates that heavy equipment rentals comprise 90% of the total. Accordingly, 2012 annual estimated rental receipts amounts to \$1.9 billion ($90\% \times \$2.1 \text{ billion} = \1.9 billion).

Based on Global Insight's industrial equipment forecast, estimated NAICS code 532412 receipts in fiscal year (FY) 2016-17 will amount to \$2.8 billion.

Property tax revenues: Staff does not have data regarding the property tax revenues heavy equipment renters currently pay. A 2013 Legislative Analyst's Office report suggests that property tax on rental equipment would likely generate between \$20 million to \$25 million annually.

Revenue Summary:

The proposed tax rate of 0.75% on \$2.8 billion in heavy equipment rental receipts would yield estimated annual revenues of \$21 million ($0.75\% \times \$2.8 \text{ billion} = \21 million).

As discussed in Page 3's comment 6, applying the 8.42% statewide average sales and use tax rate to \$21 million results in an estimated \$1.8 million state and local sales and use tax revenues annually ($8.42\% \times \$21 \text{ million} = \1.8 million).

Total revenues in FY 2016-17 is estimated to be \$22.8 million ($\$21 \text{ million} + \$1.8 \text{ million} = \22.8 million).

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