

[Assembly Bill 218](#) (Bonilla)

Date: 09/10/15

Program: Cocktail Surtax

Sponsor: Author

Part 14.5 (commencing with Section 33001), of Division 2 of the Revenue and Taxation Code (RTC)

Effective: Immediately upon enactment, but operative January 1, 2017

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This analysis is limited to the provisions which impact the Board of Equalization (BOE).

Summary: Imposes a \$0.05 per cocktail surtax on each person who purchases a cocktail from an on-sale licensee. The surtax is collected by the on-sale licensee and remitted to the BOE.

Summary of Amendments: Among the amendments since the last analysis, the bill changes the surtax operative date from January 1, 2016 to January 1, 2017 and provides the BOE with an unspecified General Fund loan for implementation costs.

Purpose: To provide funding for developmental disability services and additional health programs.

Fiscal Impact Summary: Annual revenue of \$22 million.

Existing Law: Under existing law, the Alcoholic Beverage Tax Law¹ imposes the following taxes and surcharges on the sale of beer, wine, and distilled spirits:

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

The proceeds from these taxes and surcharges are deposited into the Alcohol Beverage Control Fund and are withdrawn for use by the State's General Fund (GF) or used to pay refunds under the Alcoholic Beverage Tax program.

Proposed Law: Beginning January 1, 2017, this bill imposes a \$0.05 per cocktail surtax on every individual for each purchase of a cocktail from an on-sale licensee for consumption on their premises.

Beginning January 1, 2018, and before every January 1 thereafter, the BOE will re-compute the surtax based on the California Consumer Price Index (CPI), except that the recomputed rate shall not be less than \$0.05, and that recomputed rate applies for that calendar year.

An unspecified GF loan amount to the Fund is provided to cover BOE's implementation costs. Implementation funds are to be provided no later than six months after the bill's effective date, with the GF loan being repaid from the cocktail surtax proceeds.

¹ Sections 32151, 32201, and 32220 of Part 14 (commencing with Section 32001) of Division 2 of the Revenue and Taxation Code (RTC).

Revenues collected, less refunds, would be deposited into the Healthy California Special Fund (Fund), which this bill creates. Upon appropriation by the Legislature, moneys in the Fund will be used for developmental disability services, among other health programs, and for reimbursement to the BOE for expenses incurred in the implementation, administration, and collection of the cocktail surtax.

Definitions. This bill defines the following terms:

- “Board” means the BOE.
- “Cocktail” means any beverage that is, or contains, distilled spirits.
- “Distilled spirits” has the same meaning as that term is defined by Section 23005 of the Business and Professions Code (BPC), as in effect January 1, 2016².
- “On-sale license” means an on-sale license under the Alcoholic Beverage Control Act (Division 9 (commencing with Section 23000) of the BPC Code) that exercises the privileges described in Section 23396 of the BPC, as in effect January 1, 2016.
- “On-sale license” does not include a licensee with any of the following license types:
 - On-sale General for Train
 - On-sale General for Boat
 - On-sale General for Airplane
 - Daily on-sale General
 - Veterans’ club

On-sale licensees. On-sale licensees making sales of cocktails for consumption or use on their premises are required to register with the BOE and collect the surtax at the time of sale. The surtax is a separate charge and not included in any other fee, charge, or other amounts paid by the purchaser. The licensee must also separately state the surtax on the purchaser’s receipt or invoice. Any surtax amounts collected from the purchaser, or an amount in excess of the surtax not returned to the purchaser who paid, but collected from the purchaser under the representation that it was owed as a surtax, constitutes debts owed by the licensee to the state.

Cocktail purchaser. The cocktail purchaser is liable for the surtax until it has been paid to the BOE, except that payment to an on-sale licensee is sufficient to relieve the purchaser from further fee liability.

BOE administration. The BOE will assess and collect the tax in accordance with the Fee Collection Procedures Law (FCPL).³ The references in the FCPL to “fee” include the surtax imposed by this bill, and the reference to “feepayer” includes the person required to pay the surtax imposed by this bill.

The FCPL generally provides for the BOE’s administration of 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.

Registration of on-sale licensees required to collect the surtax shall be done in a manner prescribed by the BOE, but may include electronic media. Emergency regulation authority is also provided to the BOE.

Unless an on-sale licensee is specifically exempted, all on-sale licensees are required to collect the cocktail surtax as specified. BOE is authorized to establish procedures to be utilized by an on-sale licensee to document that alcohol consumed or used on premises are not a “purchase” subject to the cocktail surtax.

Returns. The licensee is required to file a quarterly return reporting and paying the surtax. The return is due on or before the last day of the month following the end of the quarterly period using electronic media.

² Business and Professions Code, Section 23005, defines “distilled spirits” as an alcoholic beverage obtained by the distillation of fermented agricultural products, and includes alcohol for beverage use, spirits of wine, whisky, rum, brandy, and gin, including all dilutions and mixtures thereof.

³ Part 30 (commencing with Section 55001) of Division 2 of the RTC.

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

Sales tax. This bill specifies that the cocktail surtax is not included in the definition of “gross receipts” provided in the Sales and Use Tax Law.⁴

This bill is effective immediately, but the surtax is operative January 1, 2017.

Background: In order to bridge the gap between revenues and expenses in the 1991-92 state budget, a surtax was added to the existing excise tax on alcoholic beverages. AB 30 (Chapter 86, Stats. 1991) added the alcoholic beverage surtax, codified as Section 32220, effective July 15, 1991. Before the tax increase, excise taxes on most alcoholic beverages had remained the same since the 1950s, with the exception of an increase in the excise tax on distilled spirits in 1967.

Senate Bill 248 (Romero) and Senate Bill 928 (Romero), introduced during the 2001-02 Legislative Session, would have imposed a five-cent per drink fee on any wholesaler located within the state who distributes alcoholic beverages to retailers for consumption in the state. The fee would have been based on 1.5 ounces of distilled spirits and 12 ounces of beer. Both bills would have required the proposed fee to be administered by the Department of Alcoholic Beverage Control. Both SB 248 and SB 928 failed passage in the Assembly Health Committee.

Assembly Bill 2744 (Thomson and Chan), introduced during the 2002 Legislative Session, would have increased the alcoholic beverage surtax for all alcoholic beverages in this state. AB 2744 failed passage in the Assembly Health Committee.

During the 2003-04 Legislative Session, two bills were introduced, SBx1 5 (Romero) and SB 108 (Romero), which would have imposed a five-cent per drink fee on any wholesaler located in this state who distributes alcoholic beverages to retailers for consumption in the state. The fee would be based on 1.5 ounces of distilled spirits, 12 ounces of beer, and 5 ounces of wine. Both bills passed out of the Senate Health and Human Services Committee and were referred to, and subsequently failed in the Senate Rules Committee. AB 216 (Chan), also introduced during the 2003-04 Legislative Session, would have required the BOE to collect a fee from any beer manufacturer, distilled spirits manufacturer, beer importer, and distilled spirits importer of up to \$100 million and required the DAPD to establish youth alcohol recovery and prevention programs in every county. AB 216 failed passage in the Assembly Health Committee.

SB 726 (Romero) and SB 656 (Romero) would have authorized counties, subject to voter approval, to impose a tax on the retail sale of beer, wine, or distilled spirits sold for consumption on the premises of the seller. SB 726, introduced during the 2003-04 Legislative Session, was never heard in a policy committee. SB 656, introduced during the 2005-06 Legislative Session, died in the Senate Revenue and Taxation Committee.

In the 2007-08 session, SB 297 (Romero) would have authorized a county to impose a tax on the retail sale of beer, wine or distilled spirits sold for consumption on the premises of the seller. SB 297 was never heard in committee.

During the 2009-10 First Extraordinary Session, SBx1 1 (Ducheny) was introduced to, among other things, impose an additional surtax on beer of \$0.53 per gallon, on wine of \$1.28 per gallon, and on distilled spirits of \$4.27 per gallon. SB1x 1 failed passage on the Assembly Floor. In 2009, AB 1019 (Beall) and again in 2010, AB 1694 (Beall) proposed to impose a per-gallon mitigation fee on beer, wine, and distilled spirits sold at resale by an alcoholic beverage seller, as defined. Both bills failed passage in the Assembly Health Committee.

In the 2011-12 session, SB 653 (Steinberg) would have authorized the governing board of any county or city and county, any community college district, and any county office of education, subject to specified voter approval requirements, to levy, increase, or extend certain taxes, including an alcoholic beverage tax. SB 653 died on the Senate inactive file.

⁴ Section 6012 of the Sales and Use Tax Law (Part 1 (commencing with Section 6001) of Division 2 of the RTC), generally defines the total amount of the sale, lease, or rental price, of the retail sale of the retailers. The definition goes on to specify items included and excluded from “gross receipts.”

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

Commentary:

1. **The September 10, 2015 amendments** provide for a General Fund loan for BOE implementation costs, as well as guidance to BOE to establish procedures to address alcohol purchases in certain industries. Technical amendments clarify that the surtax must be separately stated on the purchaser's receipt or invoice, provide a reference between the surtax imposed by this bill and the "fee" or "feepayer" referenced in the fee collection procedures law, as well as provide emergency regulation authority. **The September 9, 2015 amendments** changed the surtax operative date to January 1, 2017, made corresponding changes to the CPI rate computation to begin January 1, 2018, and made a non-substantive reference change to "board."

2. **Other nickel-a-drink bills imposed an equivalent amount per gallon tax on the distilled spirits at the manufacturer/wholesale level.** This bill imposes the \$0.05 surtax on the cocktail purchaser for each cocktail purchased from an on-sale licensee that is consumed on premises. The BOE would need to administer the proposed surtax as a separate tax program.

The BOE administers various tax programs, including the alcoholic beverage tax and the sales and use tax. Generally speaking, the alcohol tax is imposed on the manufacturer or wholesaler of the alcohol on a per gallon basis, while the sales tax is imposed on the retailer based on the taxable gross receipts. This bill proposes a surtax on a purchaser, with the licensee required to collect the fee. While the licensee would also be licensed with the BOE for the sales tax imposed on their taxable gross receipts, the sales tax return does not require the retailer to separately report their alcohol beverage sales subject to the sales tax.⁵ Generally, neither the licensee nor the purchaser is currently an alcoholic beverage taxpayer.

3. **While the surtax is imposed on the cocktail purchaser, the on-sale licensee will be responsible for collection.** The surtax is imposed on each purchaser of a cocktail for consumption or other use on the in-state premises of the licensee. As the bill does not exempt certain purchases, but does exempt licensees, such as those with an on-sale license for train, boat, airplane, daily, or veterans' club, all other licensees would be affected. It is unclear if certain transactions would be subject to the surtax or if there may be certain industry practices that the author should address in statute. If these issues are unresolved, the bill should at least be amended to provide the BOE broad authority to address surtax imposition and exemptions by regulation.

Some industry issues include, but are not limited to, the following: complimentary alcoholic beverages; cash or ticket bars; beverage or serving sizes; open bars; membership or private club privileges; walked checks or tabs; lump sum charges; and bad debt credits.

4. **"On-sale" licensees impacted.**⁶ By definition, the on-sale licensee does not include an on-sale general license for train, boat, or airplane operations. Additionally, a daily on-sale license and veterans' club license are also excluded from the definition.⁷ Generally speaking, the "on-sale" license refers to the sale and consumption of alcohol, including distilled spirits, on the premises of the licensee, while the "off-sale" license refers to the sale for consumption off the premises where the alcohol is sold. There are approximately 40 different types of on-sale licenses, of which only eight are commonly used and authorized to sell distilled spirits.⁸ According to ABC and BOE information, there appears to be approximately 18,000 to 20,000 on-sale licensees that would be required to register with the BOE to collect the cocktail surtax.

5. **Delayed operative date is necessary.** To effectively implement this bill, the BOE must: (1) register affected liquor licensees; (2) notify taxpayers (cocktail purchasers); (3) develop computer programs; (4) hire and train key staff; (5) create and revise necessary forms and schedules; (6) answer taxpayer and licensee inquiries; and (7) draft and adopt regulations. These functions must take place before the tax becomes operative.

⁵ The term "licensee" and "retailer" are interchangeable in discussion of the sales tax and the cocktail tax, since those alcohol retail transactions require an ABC license.

⁶ Alcoholic Beverage Control (ABC) list of license types: [California ABC - Licensees Types](#)

⁷ These include the on-sale license type numbers 53, 54, 55, 52, and 37.

⁸ These include the on-sale license type numbers 47, 48, 49, 51, 57, 70, 75, and 80.

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The bill was amended to provide a January 1, 2017 operative date, since the BOE would not have had sufficient time to implement the surtax by January 1, 2016. All BOE-computer programming resources are dedicated to the implementation of two new tax programs required by [AB 1717](#)⁹ (Perea) and [SB 84](#)¹⁰ (Budget and Fiscal Review).

- 6. Administrative start-up cost funding is essential.** This bill is effective upon enactment, but operative January 1, 2017. The BOE must begin to implement the bill prior to the cocktail surtax operative date, which requires current year funding. Without Fiscal Year 2015-16 funding, the BOE cannot begin implementation. As such, this bill authorizes a GF loan to cover upfront BOE implementation costs, to be repaid from taxes collected.

Administrative Costs: The BOE would incur substantial costs to implement a new surtax program. These costs would include developing computer programs, developing forms and publications, creating registration for licensees, carrying out compliance and audit efforts, developing regulations, training staff, and answering surtax-related inquiries from taxpayers and licensees. BOE annual costs are expected to be major (over \$1 million). In general, first year implementation costs will be the highest-cost year, with reduced ongoing costs. A detailed cost estimate is pending.

Revenue Impact:

Background, Methodology, and Assumptions. Staff research indicates that there is a limited amount of published information that would describe and provide a background about the cocktail industry in California, specifically cocktail purchases at food and drinking places. Simply stated, this bill would impose a surtax on every individual for each purchase of a cocktail from an on-sale licensee, and staff is not aware of any specific cocktail figures (such as number of drinks served or cocktail industry sales) that could be used to develop a more reliable revenue estimate.

In preparing this revenue estimate, staff analyzed four different North American Industry Classification System (NAICS) codes related to food services and drinking places. These include, NAICS 7223 Special Food Services, NAICS 7224 Drinking Places (Alcoholic Beverages), NAICS 722511 Full Services Restaurants, and NAICS 722513 Limited Service Eating Places. Based on BOE taxable sales data, total sales for these industries in 2013 was \$63 billion. Based on the most recent California Department of Finance forecast, estimated taxable sales for these industries in 2016 will be \$73 billion. To understand and estimate the cocktails or distilled spirits sales within these industries, staff analyzed the 2012 U.S. Census data for these industries, specifically the product lines data for each specific NAICS code. Staff concluded that of the \$63 billion in taxable sales in 2013, an estimated \$2.3 billion could be attributed to distilled spirits served for immediate consumption. Staff concluded that of the \$73 billion in taxable sales in 2016, an estimated \$2.6 billion could be attributable to distilled spirits served for immediate consumption.

The above analysis helped staff estimate the number of cocktails served within food services and drinking places and by using an average cocktail price, staff estimated total annual revenues of \$22 million.

Revenue Summary. Imposing a \$0.05 per cocktail surtax on each person that purchases a cocktail from an on-sale licensee would generate approximately \$22 million in revenues annually.

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

⁹ AB 1717 imposes upon each prepaid consumer a prepaid mobile telephone services surcharge to be collected by a seller on each retail transaction involving prepaid mobile telephone services.

¹⁰ SB 84 imposes a BOE-collected fee on owners of hazardous materials transported by rail in this state.

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