



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

DRAFT

Date:	05/14/13	Bill No:	Senate Bill 732
Tax Program:	Sales and Use	Author:	Berryhill
Sponsor:	Author	Code Sections:	RTC 6011 & 6012
Related Bills	SB 221 (Pavley) AB 220 (Ting) AB 1077 (Muratsuchi)	Effective Date:	Operative 90 days following 1st calendar quarter

BILL SUMMARY

This bill excludes from sales and use tax the trade-in value of a passenger vehicle for a new passenger vehicle, including a new motorcycle and pickup truck, until January 1, 2017.

Summary of Amendments

Since the previous analysis, this bill was amended to apply to motorcycles, and add the January 1, 2017, sunset date.

ANALYSIS

CURRENT LAW

Existing law¹ imposes the sales tax on retailers for the privilege of selling tangible personal property at retail in this state. The use tax is imposed upon the storage, use or other consumption in this state of tangible personal property purchased from a retailer.² The sales tax is measured by gross receipts from retail sales. The use tax is measured by the sales price of the property. Under Revenue and Taxation Code (RTC) Sections 6011 and 6012, “sales price” and “gross receipts,” respectively, are defined to include the total amount of the sale or lease or rental price, whether received in money or otherwise. The total amount of the sale, lease or rental price includes all of the following:

- Any services that are a part of the sale.
- All receipts, cash, credits and property of any kind.
- Any amount for which credit is allowed by the seller to the purchaser.

The Board of Equalization’s (BOE) Sales and Use Tax Regulation 1654, *Barter, Exchange, and “Trade-Ins,”* explains the application of tax to sales and purchases involving “trade-ins.” Subdivision (b)(1) provides that the value of a vehicle trade-in (or any other tangible personal property) may not be excluded from the computation of sales tax with respect to the property being sold for which the trade-in allowance is given. For example, if a dealer sells a new vehicle for \$20,000 and accepts a trade-in with a \$4,000 value as partial payment, sales tax is still based on the \$20,000 selling price.

¹Part 1, Division 2, Chapter 2 (commencing with Section 6051) of the Revenue and Taxation Code (RTC).
² Part 1, Division 2, Chapter 3 (commencing with Section 6201) of the RTC.

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This is also true in cases where the purchaser pays no money in the trade. For example, if a person brings a diamond ring to a jeweler and makes an even exchange for a different ring, the jeweler is required to report sales tax on the fair retail market value of the diamond ring traded in.

PROPOSED LAW

This bill amends RTC Sections 6011 and 6012 to provide that, until January 1, 2017, the terms “sales price” and “gross receipts,” respectively, do not include the value of a passenger vehicle traded in for a new passenger vehicle, including a new motorcycle or a new pickup truck, when the value of the trade-in passenger vehicle is separately stated on the new passenger vehicle invoice or bill of sale, or similar document provided to the purchaser.

This bill contains the following definitions:

- “Passenger vehicle” means any passenger vehicle as defined by Vehicle Code (VC) Section 34710, which means any motor vehicle, except any of the following:
 - Motortrucks.
 - Truck tractors.
 - Buses.
 - Housecars.
 - Specially constructed vehicles.
 - Motor vehicles constructed on a truck chassis.
 - Motor vehicles operated for hire, compensation, or profit.
 - Motor vehicles designed and constructed by the manufacturer of such vehicles, for off-highway use, as determined by the Department of Motor Vehicles.
- “Pickup truck” means a pickup truck as defined in VC Section 471, which means a motor truck with a manufacturer’s gross vehicle weight rating of less than 11,500 pounds, an unladen weight of less than 8,001 pounds, and which is equipped with an open box-type bed not exceeding 9 feet in length. “Pickup truck” does not include a motor vehicle otherwise meeting the above definition, that is equipped with a bed-mounted storage compartment unit commonly called a “utility body.”
- “Motorcycle” means a motorcycle as defined in VC Section 400, which means a motor vehicle having a seat or saddle for the use of the rider, designed to travel on not more than three wheels in contact with the ground. “Motorcycle” does not include a farm tractor.

As a tax levy, the bill takes effect immediately, but becomes operative on the first day of the first calendar quarter commencing more than 90 days after enactment.

LEGISLATIVE HISTORY

Several similar measures have been introduced over the last 14 years:

- During the 2009-10 Legislative Session, SBx6 5 (Hollingsworth), SB 658 (Walters, et al.), and SB 714 (Dutton) were held in the Senate Revenue and Taxation Committee.
- During the 2007-08 Legislative Session, SB 1417 (Hollingsworth) was also held in the Senate Revenue and Taxation Committee.

- During the 1997-98 Legislative Session, AB 1340 (Prenter & Bowler) died on the Assembly Appropriations Committee suspense file, and AB 1691 (Prenter) failed passage in the Assembly Revenue and Taxation Committee.

COMMENTS

1. **Sponsor and purpose.** The author is sponsoring this bill to provide equity with other states that provide trade-in exceptions. According to the author's office, currently, California taxpayers are expected to pay sales tax on the full price of a new vehicle purchase, even when they are providing a trade-in vehicle in lieu of a total cash payment. The state's sales tax was never designed to place a tax burden on the exchange of goods between individuals and businesses.
2. **The May 14, 2013, amendments** add new motorcycles to the proposed exemption, and incorporate a January 1, 2017, sunset date. **The April 30, 2013, amendments** specified that the proposed sales and use tax exclusion applies to the trade-in of a passenger vehicle for a new passenger vehicle, including a new pickup truck. The previous version allowed an exclusion on any motor vehicle, including motorcycles.
3. **The proposed exclusion applies to passenger vehicles and motorcycles.** The bill also specifically includes a pick-up truck with a gross vehicle weight rating of less than 11,500 pounds or an unladen weight of less than 8,001 pounds. Vehicles designed and constructed for off-highway use, as determined by the Department of Motor Vehicles, and vehicles operated for hire, compensation, or profit would not be included in the exclusion.
4. **"Motorcycle" is clearly defined in the bill.** The referenced VC Section 400 defining "motorcycle" makes it clear that the term would not include motorized bicycles, scooters, or mopeds, but would include three-wheeled motorcycles.
5. **What would be considered a "new" vehicle?** Vehicle dealers routinely use vehicles temporarily before reselling them. For example, a dealer's service department or administrative department may temporarily use vehicles as service vehicles. Some customers borrow vehicles while their own vehicles are repaired or while they await delivery of their new car. In general, a vehicle removed from resale inventory for company or customer use is subject to the use tax based on the vehicle's fair rental value for the period of such use.

Even though a vehicle may be used on a temporary basis, would the vehicle qualify as "new" for purposes of the proposed trade-in exclusion? BOE staff can assist the author's office with this concern.

6. **The bill would not apply to other common trade-in items.** While the bill limits the proposed exclusion to new vehicle trade-ins, purchasers also receive credit for other trade-in merchandise. Jewelry, appliances, tires, and car batteries are just a few examples.
7. **Suggested technical amendments.** "Passenger vehicle" defined in VC Section 34710 specifically excludes motorcycles. To avoid any confusion, we recommend the following amendment to RTC Section 6011(c)(13)(B):

"(B) Notwithstanding clause (i) of subparagraph (A), "passenger vehicle" shall include a passenger vehicle equipped with four-wheel drive and a motorcycle."

In addition, amend RTC Section 6012(c)(13)(B) to read:

“(B) Notwithstanding clause (i) of subparagraph (A), “passenger vehicle” shall include a passenger vehicle equipped with four-wheel drive and a motorcycle.”

Subdivision (c)(13) of RTC Sections 6011 and 6012 provide that the value of a *passenger vehicle* traded in for a new passenger vehicle, including a new pick-up truck or a new motorcycle, is excluded from sales and use tax. It appears that the proposed exclusion could be limited to the trade-in of a passenger vehicle only. According to the author’s office, the proposed exclusion is intended to apply to trade-ins of passenger vehicles, as well as trade-ins of pick-up trucks and motorcycles. Therefore, to avoid any confusion, we recommend the following amendment to RTC Section 6011(c) (13):

“(13) The value of a passenger vehicle, including a pickup truck or a motorcycle, traded in for a new passenger vehicle, including a new pickup truck, or a new motorcycle, if the value of the trade-in passenger vehicle, pickup truck, or motorcycle is separately stated on the new passenger vehicle, new pickup truck, or new motorcycle invoice or bill of sale or similar document provided to the purchaser.

In addition, amend RTC Section 6012(c)(13) to read:

“(13) The value of a passenger vehicle, including a pickup truck or a motorcycle, traded in for a new passenger vehicle, including a new pickup truck, or a new motorcycle, if the value of the trade-in passenger vehicle, pickup truck, or motorcycle is separately stated on the new passenger vehicle, new pickup truck, or new motorcycle invoice or bill of sale or similar document provided to the purchaser.

8. Related legislation.

- **SB 221 (Pavley)** excludes from the sales and use tax any Internal Revenue Code qualified plug-in electric vehicles tax credit, and any amount received, awarded, or allowed under a state alternative fuel vehicle incentive program.
- **AB 220 (Ting)** exempts from the state sales and use tax super ultra-low emission vehicles and advanced technology partial zero emission vehicles.
- **AB 1077 (Muratsuchi)** is identical to SB 221.

COST ESTIMATE

The BOE will incur absorbable costs to notify car dealers, audit claimed and/or netted exclusions, revise the BOE’s regulation and publications, and respond to inquiries.

REVENUE ESTIMATE

BACKGROUND, METHODOLOGY, AND ASSUMPTIONS

Vehicles. According to the *California New Car Dealers Association (CNCDA)*, an association representing franchised new car and truck dealers in California, 2.8 million new and used cars were sold by California new car dealers in 2012. Of the 2.8 million, 1.18 million were used car sales. We anticipate this bill being operative on January 1, 2014. Vehicle sales are expected to increase by 8.8% through 2014. Using this forecast, we estimate used car sales by new car dealers in 2014 to be 1.29 million vehicles.

According to *National Automobile Dealers Association (NADA)* 2012 State of the Industry report, about 35% of used cars were obtained as trade-ins on new car purchases in 2011. Applying this rate to the 1.29 million used car sales by California new car dealers, we estimate that about 452,000 vehicles will be traded in to purchase new vehicles ($35\% \times 1.29 \text{ million vehicles} = 452,000 \text{ vehicles}$).

According to NADA, the average selling price in 2012 for these used cars was \$17,300. New car dealers normally use the wholesale value of a used car when traded-in on a new vehicle. The wholesale value of the trade-in is estimated to be about 62% of the used car's retail selling price. Thus, the average trade-in value is \$10,700 ($62\% \times \$17,300 = \$10,700$).

Total trade-in value for the estimated 452,000 trade-in cars during 2014 is \$4.84 billion ($\$10,700 \times 452,000 = \4.84 billion).

Motorcycles. According to the *Motorcycle Industry Council (MIC)*, a national trade association created to promote the U.S. motorcycling industry, 318,000 on-highway motorcycles were sold in the U.S. in 2012. Based on a 12% California market share, we estimate 38,160 motorcycles were sold in the state ($318,000 \text{ U.S. motorcycles} \times 12\% = 38,160$).

Using the same 35% trade-in rate for cars, we calculate 13,356 motorcycle trade-ins ($35\% \times 38,160 = 13,356 \text{ motorcycles}$).

Since used motorcycle prices vary widely due to size, use, and aftermarket add-ons, we could not find an industry average. Therefore we estimated a 57.7% used price to new price average based on the ratio between used and new cars ($\$17,300 \text{ average used car} \div \$30,000 \text{ average new car} = 57.7\%$). According to *MIC*, the average price of a new 2012 motorcycle was \$14,692, which translates into an average used motorcycle price of \$8,477 ($\$14,692 \text{ new} \times 57.7\% = \$8,477$). Applying the same 62% average trade-in value used for cars, the average used motorcycle trade-in value is \$5,255 ($\$8,477 \text{ used price} \times 62\% \text{ trade-in value} = \$5,255$).

Total trade-in value for the estimated 13,356 trade-in motorcycle is \$70.2 million ($\$5,255 \times 13,356 = \70.2 million). Industry data shows that on-highway motorcycle sales grew by 1.8% in 2012. Assuming the same growth, the 2014 trade-in value is estimated to be \$72.7 million ($\$70.2 \text{ million} \times (1.8\% \times 2) = \72.7 million).

Vehicles and Motorcycles Trade-in. The combined car and motorcycle revenue exemption is \$4.91 billion ($\$4.84 \text{ billion trade-in cars} + \$72.7 \text{ million trade-in motorcycles} = \4.91 billion).

REVENUE SUMMARY

Assuming a January 1, 2014, operative date, the first full year revenue loss based on excluding \$4.91 billion in trade-ins from the sales and use tax is estimated to be:

Tax Exemption on Trade-ins (in millions)

Sales and Use Tax	Rate	Revenue Loss
State	4.19%	\$205.7
Fiscal Recovery Fund	0.25%	\$12.3
Local Revenue Fund	0.50%	\$24.6

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Local Public Safety Fund	0.50%	\$24.6
Local Revenue Fund 2011	1.06%	\$52.0
Local Bradley Burns	1.00%	\$49.1
Special District Tax	0.88%	\$43.2
Total Estimated Tax Loss	8.38%	\$411.5

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

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