California State
Board *of* Equalization

Legislative Bill Analysis

Legislative and Research Division

Senate Bill 1338 (Lara)
Date: 05/04/16
Program: Sales and Use Tax
Sponsor: Pacific Merchant Shipping Association
Revenue and Taxation Code Section 6377.5
Effective: Upon enactment, but operative January 1, 2017 to January 1, 2030

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Summary: From January 1, 2017 to January 1, 2030, provides a state General Fund (3.9375%) sales and use tax exemption for zero-emission or near-zero-emission equipment, including supporting infrastructure, purchased by a marine terminal operator for use primarily in, at, or on a marine terminal.

Summary of Amendments: Since the previous analysis, this bill was amended to clarify that a qualified person means an operator of a port rail ramp, rail yard, or intermodal facility, and specify the exemption applies only to off-road vehicles.

Purpose: To provide financial incentive to purchase zero-emission or near-zero-emission equipment and supporting infrastructure at California's public seaports.

Fiscal Impact Summary: Annual state General Fund sales and use tax loss of $4.6 million.

Existing Law: 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. Currently, the Sales and Use Tax Law does not provide any exemption or exclusion for sales and purchases of zero-emission or near-zero-emission equipment and vehicles for use at a California public seaport.

California's sales and use tax rates: Effective January 1, 2017, California's statewide sales and use tax rate will be 7.25%.[2] The table below shows California's various sales and use tax rate components, that will apply as of January 1, 2017 (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)
0.50%	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)
1.25%	Local (City/County) 1.00% City and County 0.25% County	(RTC Sections 7202 and 7203); City and county general operations Dedicated to county transportation purposes
7.25%	Total Statewide Rate	

[1] Part 1 of Division 2 of the Revenue and Taxation Code (RTC) (commencing with Section 6001).
[2] The 0.25% tax imposed under Section 36 of Article XIII of the State Constitution (Proposition 30, The Schools and Local Public Safety Protection Act of 2012) will sunset December 31, 2016.

Proposed Law: Beginning January 1, 2017, and until January 1, 2030, this bill provides a 3.9375% sales and use tax exemption for a "qualified person's" purchases of:

- Qualified tangible personal property to be used primarily in, at, or on a marine terminal of a California public port for carriage, handling, or movement of freight, cargo, and goods.
- Qualified tangible personal property to be used primarily to maintain, repair, measure, or test any qualified tangible personal property.

The bill provides that qualified tangible personal property includes:

  - Zero-emission or near-zero-emission equipment used in conjunction with the movement of goods or freight, including computers, data-processing equipment, and computer software required to operate, control, regulate, or maintain the qualified equipment. Qualified tangible personal property also includes repair and replacement parts for the qualified equipment.
  - Special purpose buildings and foundations used as an integral part of the utilization process of zero-emission or near-zero-emission equipment.

The bill defines the following terms:

- "Primarily" means qualified property that is used more than 50% of the time in either of the above-described activities.
- "Zero-emission or near-zero-emission equipment" means equipment, off-road vehicles, and related technologies used at a California public seaport that reduce or eliminate greenhouse gas emissions and improve air quality as identified by the State Air Resources Board in consultation with the State Energy Resources Conservation and Development Commission. Additionally, "zero-emission and near-zero-emission equipment" may include advanced or alternative fuel engines and hybrid or alternative fuel technologies for seaport equipment.

The bill defines "qualified person" as a stevedore, marine terminal operator, operator of a port rail ramp, rail yard, intermodal facility, or freight yard, or any other person that is engaged in cargo and freight loading, delivery, movement, storage, and conveyance at or within a California public seaport.

The exemption will not apply if, within one year from the date of purchase, the qualified person (1) uses the qualified property in a manner not qualifying for the exemption, (2) converts the qualified property from an exempt use to a non-qualifying use, or (3) removes the qualified property from California.

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 0.5% Local Revenue Fund, 0.5% Local Public Safety Fund, 0.25% Special Education Account Fund, and the 1.0625% Local Revenue Fund 2011.

As a tax levy, the bill takes effect immediately, but becomes operative on January 1, 2017.

Background: In July 2015, Governor Brown issued the Executive Order B-32-15 directing the California State Transportation Agency, the California Environmental Protection Agency, and the Natural Resources Agency to lead other relevant state departments, including the California Air Resources Board, the California Department of Transportation, the California Energy Commission, and the Governor's Office of Business and Economic Development, to develop an integrated action plan by July 2016. The plan must establish clear targets to improve freight efficiency, transition to zero-emission technologies, and increase competitiveness of California's freight system, which includes California's seaports.

Commentary:

1. **The May 4, 2016 amendments** (1) clarify that a qualified person means an operator of port rail ramp, rail yard, or intermodal facility, (2) specify the exemption applies only to off-road vehicles used within the boundaries of a California public seaport, and (3) add coauthors.

2. **Qualified tangible personal property.** This bill's proposed exemption for qualified tangible personal property also includes computers, data-processing equipment, computer software, devices, and component parts used to operate, maintain, repair or test the zero-emission or near-zero-emission equipment and off-road vehicles. Other qualifying property includes special purpose buildings and foundations used as an integral part of the utilization of zero-emission or near-zero-emission equipment.

   The portion subject to tax will be 3.3125%, plus applicable district-imposed taxes.

3. **Some terms need clarifying.** A qualified person includes stevedores, marine terminal operators, operators of a port, rail ramp, rail yard, intermodal facility, or freight yard, or any other person engaged in cargo and freight loading, delivery, movement, storage, and conveyance at a California public seaport. Is the proposed exemption intended to apply to any rail yard, intermodal facility, or freight yard located in California that receive cargo from a California public seaport? For example, the Intermodal Container Transfer Facility is known as a near-dock railyard located approximately five miles from the ports of Los Angeles and Long Beach. This intermodal facility transports marine cargo containers between the two Southern California container ports and major railyards near downtown Los Angeles. Would this type of intermodal facility be eligible for the exemption?

   A qualified person includes an operator of a port within a California *public* seaport. It would appear privately owned and operated ports, such as the Port of Benicia, would not qualify for the exemption.

4. **Eligible zero-emission and near-zero-emission equipment and off-road vehicles**. The bill defines zero-emission and near-zero-emission equipment as equipment and off-road vehicles used at California public seaports that reduce or eliminate greenhouse gas emissions, as identified by CARB in consultation with the State Energy Resources Conservation and Development Commission. This is a necessary requirement as BOE staff would not know the type of equipment and vehicles that qualify. According to CARB staff, zero-emission and near-zero-emission equipment and off-road vehicles include battery electric, fuel cell electric, plug-in diesel hybrid, and equipment and off-road vehicles powered by compressed natural gas. Eligible equipment and off-road vehicles include zero-emission and near-zero-emission cranes, yard trucks, top handlers, hostlers, side handlers, forklifts, loaders, aerial lifts, excavators, dozers, and more.

   In addition, the definition for zero-emission and near-zero-emission equipment includes "related technologies used at a California public seaport that reduce or eliminate greenhouse gas emissions or improve air quality." BOE staff recommends that the term "related technologies" be clarified or deleted from the bill.

5. **Eligible special purpose buildings and foundations.** Special purpose buildings and foundations used as an integral part of the process of utilization of zero-emission or near-zero-emission equipment are included in the qualified tangible personal property exemption. The bill should clarify if the proposed exemption applies to (1) buildings used to store zero-emission or near-zero-emission equipment and/or (2) buildings used solely for warehousing or storage after completion of the utilization processes.

6. **Administrative and technical concerns:**

   - In defining "qualified person," staff recommends that the bill require the qualifying person to be *primarily* engaged in the activities described. This issue generated many disputes when the BOE administered the original manufacturing sales and use tax exemption (operative from January 1, 1994 through December 31, 2003). Subsequently enacted sales and use tax exemptions all provide that a qualified person is required to be primarily engaged in the specified activities.

- The bill refers to repair and replacement parts that have a useful life of one year or more (see page 4, lines 1 and 2). The bill should provide some mechanism for determining the useful life. Current RTC Section 6377.1 provides a partial sales and use tax exemption for certain businesses engaged in manufacturing and research and development that defines "useful life" as tangible personal property having a useful life of one or more years for state income or franchise tax purposes.
- Subdivision (e) provides that the proposed exemption will not apply if, within one year from the date of purchase, the qualified person removes the qualifying property from California, converts the property from an exempt use to a non-qualifying use, or uses the property in a manner not qualifying for the exemption. However, the provision does not hold the purchaser liable for the sales or use tax if converted. BOE staff recommends amending this provision to make it consistent with RTC Section 6377.1, which specifies that the purchaser will be liable for the payment of the sales tax at the time the property is so removed, converted, or used in a non-qualifying manner exemption for manufacturing and research and development.
- Suggested amendments are detailed on page 6.

7. **Partial exemptions complicate administration.** Currently, most sales and use tax exemptions are applied to the total applicable sales and use tax. However, several partial exemptions exist in which only the state tax portion (5.25%) of the sales and use tax rate is exempted, such as the farm equipment and teleproduction equipment exemptions. These partial exemptions are difficult for both retailers and the BOE, and complicate return preparation and processing. Moreover, errors attributable to these partial exemptions occur frequently. This results in additional return processing workload for the BOE.

Costs: BOE will incur administrative costs to notify affected retailers, modify tax returns, program for the exemption's partial rate, prepare a special publication, audit claimed exemptions, and answer inquiries from taxpayers and the general public. A cost estimate is pending.

Revenue Impact:

Background, Methodology, and Assumptions. The proposed exemption is for the period January 1, 2017 to January 1, 2030. Industry sources indicate that predicting which California public seaports will be purchasing zero-emission and near-zero-emission equipment and vehicles in the future is extremely difficult, as the purchases are based on or contingent upon several factors. From the industry perspective, the state's current regulatory requirements for future purchases are unknown. Equipment purchases in the industry depend on grant funding or incentives. The technology in this area is just beginning to emerge for greater market adoption.

A December 2015 report prepared by port-planning firm Moffatt & Nichol for the Pacific Merchant Shipping Association (PMSA), which represents West Coast terminal operators and shipping lines, estimated that to replace current equipment with zero-emission or near-zero-emission equipment and vehicles, including supporting infrastructure at the ports of Los Angeles, Long Beach and Oakland, would cost $23 billion over the next 30 years.

Relative to this bill, PMSA used the above study as the basis to estimate, with certain assumptions, the average annual (2017 to 2029) zero-emission equipment purchases by the ports of Los Angeles, Long Beach, and Oakland would be $118 million.

Revenue Summary. The annual General Fund (3.9375%) revenue loss for this bill is $4.6 million (3.9375% × $118 million).

Qualifying Remarks. This revenue estimate reflects the public ports of Los Angeles, Long Beach, and Oakland, and it only includes zero-emission equipment. It does not include other ports in the state or near-zero equipment; hence, the revenue impact may be understated.

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

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.

STATE BOARD OF EQUALIZATION
PROPOSED AMENDMENTS TO SB 1338

AMENDMENT 1

On page 3, line 29, add "primarily engaged in business as" after "is" and before "a stevedore,"

AMENDMENT 2

On page 4, add new paragraph (5) after line 23 as follows:

> (5) "Useful life" for tangible personal property that is treated as having a useful life of one or more years for state income or franchise tax purposes shall be deemed to have a useful life of one or more years for purposes of this section.