Assembly Bill 2334 (Mullin, et al)
Date: 05/16/16
Program: Sales and Use Tax
Sponsor: Authors
Revenue and Taxation Code Section 6010.8 and Public Resources Code Section 26011.8
Effective: Upon enactment

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This analysis is limited to the bill's effect on the BOE-related tax programs

Summary: Increases the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) sales and use tax exclusion amount by an additional $475 million in 2016 and an additional $250 million for each calendar year thereafter. Also extends the sales and use tax exclusion to any contractor for the use in the performance of a construction contract for the participating party that will use that property as an integral part of the approved project.

Summary of Amendments: Since the previous analysis the bill was amended to add an additional coauthor.

Purpose: To expand participation in the current program by expanding the annual cap.

Fiscal Impact Summary: An additional $475 million revenue loss in 2016 and an additional $250 million each year thereafter.

Existing Law: 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, unless the law provides a specific exemption or exclusion from the sales or use tax.

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 until January 1, 2021, 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 energy source products, components or systems. In 2012, legislation was enacted[5] to authorize CAEATFA until July 1, 2016, to approve sales and use tax exclusions related to advanced manufacturing projects. The law[6] provides a $100 million cap on sales and use tax loss for these exclusions.

In 2015, legislation[7] amended the term "project" for purposes of CAEATFA's authority to approve sales and use tax exclusions for tangible personal property if at least 50% of its use is either to process recycled feedstock that is intended to be reused to produce another product or to use recycled feedstock to produce another product or soil amendment. The law specifically excludes from the term "project" tangible personal property that processes or uses recycled feedstock in a manner that constitutes disposal, as defined.

CAEATFA's approval of these exclusions is based on whether the project results in a net fiscal or environmental benefit to the State.

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[1] Part 1 of Division 2 of the Revenue and Taxation Code (RTC) (commencing with Section 6001).
[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).
[5] SB 1128 (Ch. 677, Stats. 2011, effective January 1, 2013).
[6] Public Resources Code Section 26011.8.
[7] AB 199 (Ch. 768, Stats. 2015, effective October 11, 2015).

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Construction contractors. Under the Sales and Use Tax Law, specific rules apply to the furnishing and installing of tangible personal property pursuant to a construction contract. Contracts for improvements to real property constitute construction contracts, and the person who performs the construction contract is a construction contractor. Generally, a construction contractor is the consumer of materials, such as electrical wiring, concrete, and other items, furnished and installed in the performance of a construction contract, and therefore tax generally applies to the sale of materials to the construction contractor. In contrast, a construction contractor is generally regarded as the retailer of fixtures, items which are accessory to a structure and don't lose their identity as accessories when installed, and the sales tax applies to the contractor's sale of the fixture.

Proposed Law: This bill increases the annual sales and use tax exclusion by an additional $475 million in 2016 and an additional $250 million starting in 2017 and every year thereafter, until January 1, 2021. Additionally, any amounts not granted, or amounts granted but unused from the previous calendar year, may be transferred to the following calendar year beginning in 2017.

This bill also extends the sales and use tax exclusion for approved manufacturing projects, with regard to these additional amounts, to any construction contractor for the use in the performance of a construction contract for the participating party that will use that property as an integral part of the approved project.

As a tax levy, the provisions are effective upon enactment.

Background: All applicants that apply for the sales and use tax exclusion are subject to an application and evaluation process. CAEATFA evaluates all applicants to determine whether the benefits received by the state will outweigh forgone revenue, and can only allocate exemptions to projects that produce net fiscal and environmental benefits for the state.

Commentary:

1. **This bill would expand CAEATFA's current program**. This measure would expand CAEATFA's authority to allow sales and use tax exclusions to include tangible personal property leased or purchased for a construction contract by a contractor on an approved project when the property will be an integral part of the project. The exclusion would only apply to the additional amounts added by this bill and not the $100 million currently being granted.
2. **The May 16, 2016 amendments** make non-substantive changes and add another coauthor.
3. **Adding the construction contract expansion simplifies the process**. The existing law allows the exclusion to only apply to the sale of tangible personal property to the participating party. The construction contractors do not receive the benefit of the exclusion with regard to materials consumed by them or fixtures sold from one construction contractor to another. To avoid that, every project must be structured to separate out the furnishing and installation and have all property sold directly to the participating party prior to any installation. This bill's proposed change would simplify that process. This bill extends the sales and use tax exclusion to any retail sale at any point in the chain of contracts; and the contract does not have to be specifically structured to take advantage of it.
4. **Construction contractors would need to provide an exemption certificate to retailers**. Currently, the BOE provides an exemption certificate for an approved applicant. Construction contractors would need to provide the CAEATFA application number, along with the approved recipient's contact information and to supply the certificate to the vendor to receive the sales and use tax exclusion.
5. **The sales and use tax exclusion's administration falls primarily under the CAEATFA.** As a result, the BOE's administrative duties would be minimal.

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6. **Related legislation.** Assembly Bill 1683 (Eggman) allows the unallocated portion of the current $100 million cap in one calendar year to be added to the following calendar year's cap.

Costs: The BOE would incur some absorbable costs to notify taxpayers, change the BOE's website and publications, and answer inquiries.

Revenue Impact: This bill expands the allowable sales and use tax exclusion for all projects approved by CAEATFA by $475 million in 2016 and $250 million each year thereafter, with a rollover of the unused portion for one calendar year. Between November 2010 and January 1, 2016, CAEATFA has approved tax exclusions of about $455 million, but only $92 million in tax has actually been claimed.[8]

[8] California State Treasurer. (2016, January 1). Retrieved March 8, 2016, from http://www.treasurer.ca.gov/caeatfa/ste/applicants/considered.pdf