DRAFT

STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date:	**02/21/14**	Bill No:	**Assembly Bill 2691**
Tax Program:	**Sales and Use**	Author:	**Harkey**
Sponsor:	**Author**	Code Sections:	**RTC 6012.4**
Related Bills:		Effective Date:	**Upon enactment**

BILL SUMMARY

This bill specifies that the "gross receipts" and "sales price" from the retail sale of a wireless telecommunication device (device) are limited to the amount charged for the device when it is sold in a bundled transaction, as defined.

ANALYSIS

CURRENT 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.

The law[2] defines the terms "gross receipts" and "sales price" as the total amount of the sale or lease or rental price without any deduction for the material cost, labor or service costs, interest charged, losses, or any other expenses related to the property's sale. Normally, the law regards a service sold in connection with a taxable good as part of the sale. Accordingly, the tax is based on the total receipts derived from that sale.

However, the marketing and retail pricing strategies associated with these devices and the telecommunications industry contradict conventional and customary retail practices. As a result, in 1999, the Board of Equalization (BOE) adopted a regulation[3] to specifically address the tax application on these device sales and related service charges.

Under the regulation, retailers are required to compute the tax based on whether they sold the device in a "bundled" or "unbundled" transaction. The regulation defines "bundled" transactions as those sales where the customer is required to activate or contract for utility service with a wireless telecommunications service provider for a one-month period or greater as a sale condition. Generally, to receive the device's promotional or discounted sales price, customers must agree to activate or sign up with a provider for utility service for more than a one-month period. Under the regulation, generally, the retailer is required to compute tax on the device's sale based on the "unbundled sales price."

The regulation further defines "unbundled sales price" as the price at which the retailer has sold specific device types to customers who are *not* required to activate or contract for utility service as a condition of sale. If the retailer has not previously sold a specific

---

[1] Part 1, Division 2 (commencing with Section 6001) of the Revenue and Taxation Code (RTC).
[2] RTC Sections 6011 and 6012, respectively.
[3] Regulation 1585, *Cellular Telephones, Pagers, and other Wireless Telecommunications Device.*

device in other than a bundled transaction, the unbundled sales price is equal to the devices' fair retail selling price.

If the sale is unbundled (the customer is not required to activate or contract for utility service as a condition of sale), the tax applies to the devices' actual sale amount to the customer.

PROPOSED LAW

This bill adds RTC Section 6012.4 to the Sales and Use Tax Law to provide that the terms "gross receipts" and "sales price" from the retail sale of a wireless communication device shall be limited to the amount charged for the device when it is sold in a bundled transaction, as defined.

The bill defines "bundled transaction," "wireless telecommunications device," and "wireless telecommunications provider."

As a tax levy, the bill would become effective immediately.

BACKGROUND

In the past, three similar bills[4] have been considered, but none were approved. The Assembly bills were held in the Assembly Revenue and Taxation Committee, and the former Senate bill failed in the Senate Committee on Governance and Finance.

COMMENTS

1. **Sponsor and Purpose.** Assembly Member Harkey sponsors this measure to minimize the confusion consumers experience about the tax amount when they buy cell phones and other devices in a bundled transaction. The author's office believes that the specific amount charged for the device's sale should only be the amount upon which tax is based.

2. **This measure's enactment would lessen purchasers' confusion.** Purchasers are generally accustomed to paying sales tax reimbursement to retailers based on the goods' purchase price. For these devices, however, the BOE receives numerous purchaser inquiries regarding the sales tax retailers charge in connection with contracts involving purchases of these devices, since the tax is computed so differently. This measure's enactment would minimize these inquiries.

3. **Bill only applies prospectively.** Retailers have relied on the BOE's applicable regulation to report their tax liabilities and it is our understanding that this legislation is not intended to have a retroactive effect.

4. **Bill should contain a delayed operative date.** The bill provides no lead time for the BOE to notify affected retailers and provide instructions related to their reporting obligations. Page 4 of this analysis contains a suggested amendment to provide the necessary lead time.

[4] SB 1086 (Dutton and Garrick, 2012), AB 279 (Garrick, 2011), and AB 2320 (La Malfa, 2005-06).

COST ESTIMATE

The BOE would incur absorbable costs to administer this bill. These costs would be attributable to notifying affected retailers, revising the BOE's regulation, revising publications, and answering inquiries from taxpayers and the public.

REVENUE ESTIMATE

According to statistics compiled by mobiThinking.com, we estimate that the 2013 United States wireless handset market amounted to approximately $48 billion.

Based on a survey of the largest wireless providers, the average sales price of a separately sold handset is $482.91, and the average price of a handset sold in a bundled transaction is $101.16. Therefore, the average sales price for a handset amounted to 21% of the average sales price ($101.66/$482.91 = 21%). For this estimate, we assume that the average sales price for wireless devices sold in bundled transactions is 21% of the sales price of these devices sold separately. Accordingly, the estimated annual revenue loss is calculated as follows:

Revenue Summary	Annual Sales 000's
US Handset Sales	$ 48,000,000
California Sales: (12% of US sales)	5,760,000
Proposed Taxable Measure (21%)	1,209,600
Foregone Taxable Measure	4,550,400
Estimated State and Local Revenue Loss (8.42%)	$ 383,144

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

Analysis prepared by:	Sheila Waters	916-445-6579	04/29/14
Revenue estimate by:	Bill Benson	916-445-0840	
Contact:	Michele Pielsticker	916-322-2376	

ls 2691ab022114stw.docx

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 Board's formal position.

STATE BOARD OF EQUALIZATION
PROPOSED AMENDMENTS TO AB 2691

On page 3, line 6, after "effect." insert the following:

However, Section 1 shall become operative on the first day of the first calendar quarter commencing more than 90 days after the effective date of this act.