



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE ENROLLED BILL ANALYSIS

Date Amended:	Vetoed	Bill No:	AB 1087
Tax:	Sales and Use	Author:	Ma
Related Bills:			

BILL SUMMARY

This bill would specify that, with respect to delivery charges made by retailers in connection with a taxable sale of tangible personal property, if those charges are not separately stated, or if they are combined with handling or other charges, then the exclusion from the computation of sales and use tax for those charges would not apply.

ANALYSIS

CURRENT LAW

Under existing law, Revenue and Taxation Code Sections 6011 and 6012 imposes the sales or use tax on all charges related to the retail sale of tangible personal property except those charges specifically excluded from taxation by statute.

Paragraphs (7) of subdivision (c) of these statutes, provides an exclusion from taxable "sales price" and "gross receipts" for separately stated charges for transportation from the retailer's place of business or other point from which shipment is made directly to the purchaser. This exclusion, however, may not exceed a reasonable charge for transportation by facilities of the retailer or the cost to the retailer of transportation by other than facilities of the retailer. If the transportation is by facilities of the retailer, or the property is sold for a delivered price, this exclusion is applicable solely with respect to transportation that occurs *after* the sale of the property is made to the purchaser.

Paragraphs (2) of subdivision (a) of these statutes specify that taxable "sales price" or "gross receipts" include the cost of services that are part of the sale of tangible personal property. Therefore, charges for handling related to the sale of tangible personal property are taxable whether separately stated or not. Thus, under existing law, a charge for "shipping and handling" is not a separate statement of shipping charges. If there is no further itemization, the charge for shipping and handling would not constitute a separate statement of transportation charges and the entire charge would be included in the computation of sales or use tax.

Although a designation such as, "shipping and handling" or "postage and handling" is not regarded as a separate statement of transportation charges, under the Board's Regulation 1628, *Transportation Charges*, if a separately stated charge is made for "postage and handling," "shipping and handling," or similar designation, that portion of the charge which represents actual postage or actual shipment may be excluded from the tax. However, to be excluded from tax, the retailer must maintain records showing the actual cost of transportation for each individual transaction.

If the actual amount paid to the carrier is not clearly supported in the retailer's records, then the full amount of the "shipping and handling" charges are taxable.

Transportation and handling charges, or any other service charges made in connection with nontaxable transactions, however, are nontaxable.

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.

PROPOSED LAW

This bill would amend Revenue and Taxation Code Sections 6011 and 6012 to specify that charges for transportation are separately stated for the purposes of the exclusion if those charges are stated as a single amount and are not included within a single amount that combines transportation charges with other charges.

The bill would become effective January 1, 2010.

IN GENERAL

Both retailers and purchasers have difficulty understanding the application of tax to transportation charges. This is especially so because one of the requirements for the exclusion for separately stated transportation charges is that the cost of transportation must be the actual shipping cost. This actual shipping cost is determined on a transaction-by-transaction basis. Thus, to be entitled to the exclusion, in addition to separately stating the transportation charge, retailers must keep records showing the actual cost of transportation for each transaction. The amount of each individual cost of transportation is then the amount excludable.

With respect to on-line transactions, many retailers simply add an average or standard charge for transportation, and do not charge the "actual" cost or show a separate statement of the "actual" cost. In so doing, the transportation charges are required to be included in the amount subject to tax. Other retailers that charge the actual cost of shipping and meet the conditions of the exclusion are burdened by the necessity of maintaining detailed records to support a claimed deduction for excluded charges for transportation. Also, customers have difficulty understanding why they are charged tax on transportation charges in some cases and not in others.

COMMENTS

- 1. Sponsor and purpose.** The sponsor of this bill is the California Retailer's Association. Its purpose is to simplify the law as it relates to transportation charges by specifying that if the transportation charges are combined with handling or other charges, then the transportation charges would become subject to sales or use tax, regardless of whether they are separately stated.
- 2. Key amendments.** The September 2, 2009 amendments incorporated an unrelated provision that amends the Public Contracts Code that is outside the Board's purview. The June 1, 2009 amendments specified that charges for transportation are separately stated for the purposes of the exclusion if those charges are stated as a single amount and are not included within a single amount that combines transportation charges with other charges. The amendments also changed the vote requirement on the bill from 2/3 to majority and deleted the provisions that would have made the bill operative on the first day of the calendar quarter commencing more than 90 days after the effective date of the bill.

- 3. How does this version differ from current interpretations?** Currently, if a charge for delivery is combined with a charge for handling or other service charge, the charge for the delivery may be excluded from the computation of sales or use tax as long as the “postage and handling” or “shipping and handling” or other shipping designation is shown on the retailer’s invoice, and the actual amount of the postage or shipping is documented in the retailer’s records. This bill would require that in such cases, the entire postage or shipping charge (including any other service charge) would be included in the computation of sales or use tax.
- 4. How is this version of the bill different from the previous?** Although the bill is no longer keyed a fiscal measure, it is unclear how the June 1, 2009 amendments change the overall effect of the bill. It appears these amendments would accomplish the same result as the previous version, and that a revenue increase would continue to occur to the extent that those retailers that currently exclude the transportation charges from the computation of sales or use tax would no longer be able to under the provisions of the bill.
- 5. This may be consistent with how these charges are treated by some retailers already.** The application of sales and use tax to combined shipping and handling charges or to flat-rate or estimated shipping charges has been the source of confusion for a variety of retailers. For simplicity purposes, some calculate the tax based on the entire charge, regardless of whether there is a separate statement of the actual shipping charge or whether records showing the actual cost of shipping are maintained. For those retailers, this bill would be consistent with their reporting habits. For others, this bill would simplify record-keeping requirements.
- 6. This bill would assist consumers in proper reporting of use tax on shipping charges.** Currently, when a consumer makes a taxable purchase from an out-of-state retailer that is not registered with the Board to collect use tax, the consumer is liable for the use tax on the purchase. The consumer may report his or her use tax to the Board or on the consumer’s state income tax return. The use tax is due on the sales price of the property, and on any taxable shipping charges or other service charges associated with the sale of that property. In cases where a charge for “shipping and handling” is shown on the consumer’s receipt, it can be difficult for a consumer to determine the actual amount of shipping that the consumer may exclude from his or her computation of use tax. Enactment of this bill would eliminate this difficulty, as the entire charge would be subject to use tax.

COST ESTIMATE

Some administrative costs would be incurred in notifying taxpayers, revising Regulation 1628, and related Board publications and manuals. These costs would be offset by the decrease in audit hours spent in verifying claimed exclusions related to transportation charges of retailers.

REVENUE ESTIMATE

Using the North American Industry Classification System, we estimate that courier shipping charges, excluding the U.S. Postal Service (USPS), amounted to an estimated \$805 million in California in 2007. Based on statistics compiled using USPS data, we estimate that only 70%, or \$564 million, of these charges are for package delivery; the remainder would be attributable to document delivery. Using operating statistics from USPS, we estimate that package delivery from the USPS amounted to approximately

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\$277 million in California in 2007. The total for all delivery charges in California amounted to an estimated \$841 million (\$564 million + \$277 million) in 2007. We know that retailers collect and remit tax reimbursement for a portion of these charges under current law and industry practice. In addition, private citizens send packages via the USPS and private delivery companies. If half of these delivery charges are not currently taxable or reimbursed, the amount of state and local revenue associated with all nontaxable delivery charges under current law would amount to \$37.8 million (50% x 841 million x 9%).

We do not have precise information on the percentage of the \$37.8 million charges that this measure would affect. However, if we assume that one-tenth of the currently excluded transportation charges would be subject to tax under this measure, the annual increase in state and local sales and use tax would amount to \$3.78 million, as follows:

State General Fund (6%)	\$2,520,000
State Fiscal Recovery Fund (1/4%)	105,000
Local (2%)	840,000
Special districts (.75%)	<u>315,000</u>
Total	<u>\$3,780,000</u>

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