



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

Date Introduced:	02/20/01	Bill No:	AB 375
Tax:	Sales and Use	Author:	J. Campbell
Board Position:	Neutral	Related Bills:	

BILL SUMMARY

This bill would provide an exemption from the use tax for the first \$500 in purchases that would otherwise be subject to the use tax.

ANALYSIS

Current Law

Under existing law, sales tax is imposed on retailers for the privilege of selling tangible personal property at retail in this state. A use tax is imposed on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer. Generally, the use tax applies to a sale or purchase when the sales tax does not. For example, property purchased from an out-of-state vendor will generally be subject to the use tax rather than the sales tax. Some out-of-state vendors are registered with the Board for the purpose of collecting and remitting the use tax that is due on their sales to California consumers.

Current law provides that the storage, use, or other consumption in this state of the first \$400 of tangible personal property purchased in a foreign country by an individual from a retailer and personally hand carried into this state from the foreign country within any 30-day period is exempt from the use tax. The \$400 use tax exemption does not apply to property sent or shipped to this state.

Proposed Law

This bill would add Section 6405.1 to the Sales and Use Tax Law to provide that the storage, use, or other consumption in this state of the first \$500 of tangible personal property, which would otherwise be subject to the use tax, is exempted from the use tax. The proposed exemption would be in addition to the \$400 use tax exemption allowed for items purchased from a foreign country and personally hand carried into this state.

This bill also provides that the proposed use tax exemption would not apply to tangible personal property leased in substantially the same form as acquired by the lessor.

The provisions of the bill would become operative immediately.

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.

COMMENTS

1. **Sponsor and purpose.** According to the author's office, who is also the sponsor, the purpose of this bill is to provide a use tax exemption on the first \$500 in purchases so that a business may enjoy the benefits of tax free purchases like many individuals currently enjoy.
2. **Who pays use tax.** Current law requires that a purchaser of tangible personal property from a retailer pay use tax to the state if sales tax does not apply. Generally, this type of transaction consists of purchases from out-of-state vendors. If the purchaser holds a permit with the Board of Equalization, purchases subject to use tax should be reported and the use tax paid to the state. Permit holders are subject to audit, and purchases subject to use tax are commonly assessed. If the purchaser does not hold a permit with the Board of Equalization, the use tax generally goes unpaid. Due to the cost of collection associated with each transaction, the Board does not generally pursue the use tax due on individual purchases by persons who do not hold a permit with the Board. Also, there is generally a lack of knowledge by the purchaser that any tax is due. However, any person who purchases tangible personal property from out-of-state may voluntarily remit the proper use tax to the state.
3. **California based retailers could be adversely affected by the proposed use tax exemption.** By creating a use tax exemption, purchasers would be encouraged to purchase tangible personal property from out-of-state locations. Some out-of-state vendors currently collect use tax on sales made to California consumers, but this bill would create an exemption for purchases from any out-of-state vendor.
4. **Use tax exemption would apply to some used car sales.** In addition to applying to purchases from out-of-state vendors, use tax applies to purchases of vehicles, vessels and aircraft when purchased from someone other than a retailer. As currently written, a used car purchased from a car dealer would be subject to tax on the full purchase price (sales tax), while a used car purchased from a private party would be subject to tax on the full purchase price less \$500 (use tax).
5. **Proposed exemption would apply to first \$500 in purchases each year.** Although not currently outlined in the bill, the author's office indicated the \$500 in purchases subject to use tax is intended to apply to the first \$500 in purchases per person each year.
6. **Provisions of this bill would be difficult to administer.** The proposed exemption would apply to the first \$500 in purchases subject to use tax per person per year. Retailers collecting use tax would have no way of knowing the dollar amount of tangible personal property previously purchased by a person when computing the amount subject to tax on a current sale. The Board would also have a difficult time establishing whether a particular sale would qualify for the exemption, so verification of claimed exempt sales would be complicated.

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COST ESTIMATE

Some absorbable costs would be incurred in revising publications and notifying the public and Board staff. However, the workload and associated costs for processing claim exemptions and reviewing returns to ensure that the taxpayers do not exceed the \$500 annual limitation is undeterminable at this time.

REVENUE ESTIMATE**Background, Methodology, and Assumptions**

According to the author's office, this bill would exempt from the use tax the first \$500, on an annual basis, of tangible personal property which would otherwise be subject to the use tax. Use tax is collected from a variety of taxpayers.

Vehicles, vessels and aircraft purchased from out-of-state sellers and brought into California for use or in-state purchases from non-dealers are subject to the use tax. When consumers register vehicles or undocumented vessels purchased from non-dealers or from out-of-state, they are responsible for the payment of the use tax to the DMV at the time of registration. During fiscal year 1999-2000, the DMV collected use tax on 1,940,292 such vehicles and vessels. The average use tax liability on these purchases was about \$3,200. In addition, the purchase of a mobilehome from non-California dealers is reported to the state Housing and Community Development Department (HCD). HCD collects the use tax on these mobilehomes. During fiscal year 1999-2000, HCD collected use tax on 15,464 such mobilehomes.

The tax due upon the purchase of a documented vessel or an aircraft from a non-retailer or from outside the state is payable directly to the Board. These payments are processed by the Board's Consumer Use Tax Section (CUTS). CUTS also has responsibility for the Board's Customs Declaration Program. CUTS obtains from the U.S. Customs Service copies of the personal declaration forms completed by California residents upon returning from foreign destinations. These forms disclose the value/purchase price of property purchased in foreign countries and brought back into California for use. Under Revenue and Taxation Code Section 6405, the first \$400 of tangible personal property purchased in a foreign country and hand carried into California within a 30-day period, is exempt from use tax. This proposed exemption would be in addition to the Section 6405 exemption. During fiscal year 1999-2000, CUTS collected use tax from 11,482 consumers.

Out-of-state retailers that are "engaged in business" in California or that voluntarily register to collect the tax even without "nexus" in California are issued a Certificate of Registration. Currently, 12,584 such businesses have a Certificate of Registration. These businesses do not report to the Board the number of taxpayers from whom they collect use tax. In order to estimate the possible revenue impact of this proposal, we will assume that each of these businesses collects use tax from 100 California consumers. The estimated total number of consumers would be 1,258,400.

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In-state businesses, which have sales and use tax permits with the Board, are required to report purchases that are subject to use tax on their sales tax returns. Annually about 44,000 businesses report such use tax liabilities.

All of the above taxpayers would be eligible for the proposed use tax exemption on the first \$500. The use tax revenue on \$500 at the effective tax rate of 7.92% amounts to \$39.40. It is assumed that all of the above taxpayers would have a use tax liability of at least that much. The estimated number of taxpayers and use tax liability would be as follows:

<u>Category</u>	<u>Taxpayers</u>	<u>Exempt Amount</u>	<u>Total Exemption</u>
DMV	1,940,292	\$500	\$ 970.1 million
HCD	15,464	500	7.7 million
CUTS	11,482	500	5.7 million
Cert. Of Reg.	1,258,400	500	629.2 million
Sales Tax Returns	<u>44,000</u>	<u>500</u>	<u>22.0 million</u>
Total	<u>3,269,638</u>		<u>\$1,634.7 million</u>

Revenue Summary

The annual revenue loss from exempting from the use tax the first \$500 of tangible personal property which would otherwise be subject to use tax would be as follows:

	<u>Revenue Loss</u>
State loss (5%)*	\$ 81.7 million
Local loss (2.25%)	36.8 million
Transit loss (0.67%)	<u>11.0 million</u>
Total	<u>\$ 129.5 million</u>

* While the state tax rate is 4.75 percent for calendar year 2001, it is assumed the tax rate will return to 5.0 percent in 2002.

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Qualifying Remarks

This proposal would preclude the Board from attempting to collect use tax on the first \$500 of use tax liability from individual consumers. Other than the situations detailed above, the Board historically has not attempted to collect use tax directly from individual consumers, because it has not been cost effective to do so. The proposed partial exemption of such uncollected use tax liabilities would not result in any loss of current revenue but could mean a loss of future revenues if cost effective means of collection became available.

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