



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

Date Amended:	05/16/01	Bill No:	AB 904
Tax:	Sales and Use	Author:	Briggs
Board Position:	Oppose	Related Bills:	

BILL SUMMARY

This bill would provide a *state* (5%) sales and use tax exemption for the sale and purchase of any thoroughbred horse breeding stock.

ANALYSIS

Current Law

The existing Sales and Use Tax Law imposes a tax on the sale of, or the storage, use, or other consumption in this state of, tangible personal property, unless that property is specifically exempted or excluded by statute. Generally, sales of horses and any other animals are subject to tax to the same extent as any other sales of tangible personal property. However, existing law does provide the following exemptions or exclusions with respect to sales and other types of transfers of animals:

- Section 6010.40 excludes from the computation of sales and use tax any receipts associated with the transfer by a local government animal shelter or a nonprofit animal welfare organization of any animal to an individual for use as a pet.
- Section 6358 provides an exemption for the sale or purchase of any form of animal life the products of which ordinarily constitute food for human consumption (e.g., sales and purchases of cows, bees, and chickens are exempt from tax).
- Section 6366.5 provides an exemption for the sale and purchase of endangered or threatened animal and plant species if both the seller and the purchaser are nonprofit zoological societies.

For purposes of establishing whether a horse is subject to ad valorem property tax or to the race horse in lieu tax, the Board's Property Tax Rule 1046 provides in part that a horse used for breeding purposes means a registered male animal that has serviced three or more registered females for the purpose of producing a racehorse during the two previous calendar years or a registered female animal that has been bred to a registered male for the purpose of producing a racehorse during the two previous calendar years.

Currently, a base state and local sales and use tax rate of 7 percent is imposed as noted below:

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- 4 3/4 percent state tax allocated to the state's General Fund (this rate is expected to increase to 5 percent on January 1, 2002) (Sections 6051 and 6201).
- 1/2 percent state tax allocated to the Local Revenue Fund which is dedicated to local governments for program realignment (Sections 6051.2 and 6201.2).
- 1/2 percent state tax allocated to the Local Public Safety Fund which is dedicated to local governments to fund public safety services (Sec. 35 of Article XIII of the California Constitution).
- 1 1/4 percent Bradley-Burns Uniform Local Sales and Use Tax which is allocated to cities and counties (Part 1.5 (commencing with Section 7200)).

An additional local district tax ranging from 1/8 to 1 1/4 percent (referred to as Transactions and Use taxes) is imposed by special taxing jurisdictions in various counties and cities within the state (Part 1.6 (commencing with Section 7252)).

Proposed Law

This bill would add Section 6358.5 to the Sales and Use Tax Law to exempt from the state sales and use tax rate, the sale and purchase of any thoroughbred horse breeding stock.

The bill would define "thoroughbred horse breeding stock" to mean a horse that is capable of reproduction and for which the purchaser states that it is the purchaser's sole intent to use the horse for breeding purposes.

The bill would become effective immediately, but would become operative on the first day of the calendar quarter commencing more than 90 days after the date the bill is enacted.

Background

Other bills proposing to provide an exemption for thoroughbred horses have been considered in the past. AB 2757 (Wright) of the 1987-88 Legislative Session would have provided an exemption similar to this measure, and would have additionally exempted receipts attributable to stallion services, sales of thoroughbred horses less than two years of age sold to an out-of-state resident that are transported outside California, receipts for boarding and training thoroughbred horses, and the temporary use of thoroughbred horses within this state for purposes of racing, exhibiting, or performing. AB 2679 (Wright) of the 1986-87 session would have created an exemption for the sale and purchase of a thoroughbred horse or an Arabian horse which is used as breeding stock.

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COMMENTS

1. **Sponsor and Purpose.** According to the author's office, the sponsor of this measure is the California Thoroughbred Breeders Association. Its purpose is to assist California purchasers who wish to acquire breeding stock without the added expense of tax on their acquisitions.
2. **The May 16, 2001 amendments define "thoroughbred horse breeding stock."** This amendment appears to address the comment raised in the Board's earlier analysis that, absent a definition, the seller and purchaser could argue that virtually all sales of thoroughbreds, except for geldings, qualify for the exemption.
3. **The April 16, 2001 amendments eliminate local taxes from the proposed exemption.** Therefore, the exemption would only apply to the state tax portion of the sales and use tax rate, currently 4 $\frac{3}{4}$ percent (the rate is expected to increase to 5 percent beginning January 1, 2002).
4. **Proponents view this measure as an enhancement to revenues and an opportunity to make California a more friendly place to the race horse industry.** Proponents of the measure point out that this measure could ultimately enhance the sales and use tax base, since an incentive would be created to breed more horses for racing purposes. Since the final sale of a race horse would remain subject to tax, California's sales and use tax revenues would actually be enhanced. As an example, a horse bred to race may be sold as a yearling for \$3,000 and then compete as a race horse at a value of \$10,000. According to statistics maintained by The Jockey Club, the State of Kentucky annually leads the list of states producing registered thoroughbred foals, consistently increasing its share in recent years. From the top 12 foal producing states, only Kentucky, Florida, and Pennsylvania have produced more registered foals in 1999 than at the start of the decade. For more than a quarter of a century, since The Jockey Club began computerized analysis of the foal crop, Kentucky has been followed by California and Florida. In 1994, however, Florida overtook California to become the nation's second largest producer of registered thoroughbred foals. Under Kentucky's Sales and Use Tax Law, all sales of horses are exempt from tax. Florida exempts the sale of a race horse by its owner provided the owner is also the breeder of the animal. Proponents of this measure see this bill as an opportunity to "spur" the race horse industry in California and to make California's tax climate more competitive with the two leading states in the production of registered thoroughbred foals.

COST ESTIMATE

Some costs would be incurred in notifying affected taxpayers, answering inquiries, and reviewing claimed exemptions on returns. These costs are expected to be absorbable.

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REVENUE ESTIMATE

Background, Methodology, and Assumptions

There are a number of sales conducted annually by only a few organizations: Barretts, American Equine, and the California Thoroughbred Breeders Association. The largest of those organizations is Barretts, an auction company that makes four sales per year. Sales of thoroughbred horses include yearlings, two-year olds, and two-year olds in training. It is assumed that any thoroughbred horse except for geldings could be used as breeding stock. Sales of thoroughbred horses for the year 2000 are comprised of the following:

Del Mar Yearling Sale	\$ 4.1 million
Barretts	
January Sale	\$ 2.1 million
March Sales	\$17.3 million
May Two-Year-Olds in Training	\$ 5.0 million
October Mixed Sales	\$ 2.7 million
American Equine	<u>\$ 0.8 million</u>
Total	<u>\$32.0 million</u>

Revenue Summary

The annual revenue loss from exempting \$32 million from the 5 percent* state sales and use tax is estimated to be \$1.6 million.

* 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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