



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

Date Introduced:	02/23/01	Bill No:	AB 1601
Tax:	Sales and Use	Author:	Papan
Board Position:		Related Bills:	AB 646 (Horton) AB 811 (Zettel)

BILL SUMMARY

This bill would specify that certain disposable surgery gowns are “medicines” for purposes of exempting the sale of these items to a health facility.

ANALYSIS

Current Law

Under existing law, sales or use tax applies to all sales or purchases of tangible personal property, unless otherwise exempted or excluded from the computation of sales or use tax. Section 6369 of the Sales and Use Tax Law provides an exemption from tax for the sale and use of medicines sold to a licensed physician and surgeon, podiatrist, dentist, or health facility for the treatment of a human being. This section provides a comprehensive description of items included and excluded from the term “medicine.” For example, this section specifies that the following items are *excluded* from the term “medicine”: articles that are in the nature of splints, bandages, pads, compresses, supports, dressings, instruments, apparatus, contrivances, appliances, devices, or other mechanical, electronic, optical, or physical equipment or article or the component parts and accessories thereof.

Under the Sales and Use Tax Law, generally, persons engaged in the business of providing laundering services are the consumers of linen supplies and similar articles, including such items as towels, uniforms, coveralls, dust cloths and surgical gowns rented to others when an essential part of the rental contract is the furnishing of the recurring service of laundering or cleaning of the articles rented. As consumers, tax does not apply to the launderers’ or cleaners’ charges for the furnishing and cleaning the articles, but rather, tax applies with respect to the launderers’ or cleaners’ purchase of the articles. On the other hand, persons who make sales of such items as disposable surgical gowns to hospitals, or to any other purchaser, are required to remit tax on his or her sales to the same extent as any other retailer making retail sales of tangible personal property.

Proposed Law

This bill would amend Section 6369 of the Sales and Use Tax Law to include within the term “medicines” disposable surgery gowns made from nonwoven fabric, thereby effectively exempting the sale of these items to hospitals and other health facilities.

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.

The bill would become operative on the first day of the calendar quarter commencing more than 90 days from the date the bill is enacted.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by INDA, Association of the Nonwoven Fabrics Industry. According to the author's office, its purpose is to create a level playing field between providers of disposable surgical gowns and providers of reusable gowns.
2. **It is recommended that a separate statute contain the proposed exemption, rather than Section 6369.** The sale and purchase of qualifying "medicines" described in Section 6369 are exempt when sold to health facilities provided they are for the "treatment" of a human being. It could be argued that a surgical gown itself does not actually contribute to the "treatment" of a human being and therefore, the proposed exemption would not apply. In order to avoid any ambiguity with administration of the proposed exemption, the author may wish to amend the bill to create this exemption under a statute of its own.
3. **Would enactment of this bill create a level playing field?** While the rental charges that a reusable surgical gown launderer/provider receives are excludable from the computation of sales or use tax, the launderer is required under the law to pay tax on his or her purchase price of the surgical gowns. This measure, on the other hand, would enable a disposable surgical gown provider to receive the benefit of a complete exemption – no tax would be required to be paid on his or her acquisition costs of the gowns, nor would tax be required to be paid on the subsequent sale of the gowns to the health facility. It could be argued that enactment of this measure would actually provide disposable surgical gown suppliers with a tax advantage over reusable gown suppliers.
4. **Related legislation.** There are currently two other measures introduced this session that would amend Section 6369:
AB 646 (Horton), which is a Board-sponsored measure, would specify that sales of medicines to clinics, as defined, for the treatment of any person pursuant to the order of a licensed physician and surgeon, dentist, and podiatrist are exempt from sales and use tax.
AB 811 (Zettel), which would provide a sales and use tax for the following items when furnished by a health facility for treatment of any person pursuant to an order of a licensed physician, surgeon, dentist, or podiatrist:
 - (1) Any auditory, prosthetic, ophthalmic, or ocular device or appliance.
 - (2) Articles that are in the nature of splints, bandages, pads, compresses, supports, dressings, instruments, apparatus, contrivances, appliances, devices, or other mechanical, electronic, optical, or physical equipment or article or the component parts and accessories thereof.
 - (3) Alcoholic beverages.

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COST ESTIMATE

Administrative costs would include providing notices to affected retailers, auditing claimed exemptions, and amending the Board’s regulation. These costs are expected to be absorbable.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

This bill would exempt disposable surgical gowns made from nonwoven fabric from the sales and use tax. According to industry sources, 2000 U.S. sales of nonwoven surgical gowns is estimated to be \$200 million. Assuming that California accounts for 12% of those sales (the percentage of population California represents of total U.S. population), the estimated 2000 sales that qualify under this proposal are estimated to be \$24 million (\$200 million x .12).

Revenue Estimate

The revenue impact from exempting the \$24 million in sales of nonwoven surgical gowns from the sales and use tax would be as follows:

	Revenue Loss
State (5.00%)**	\$ 1.2 million
Local (2.25%)	\$.5 million
Special Districts (0.67%)	<u>\$.2 million</u>
Total	\$ 1.9 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.

Analysis prepared by:	Sheila T. Sarem	445-6579	04/06/01
Contact:	Margaret S. Shedd	322-2376	

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