

Tax Information Bulletin

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California State Board of Equalization
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Don't forget to report your purchases subject to use tax

Use tax is receiving a lot of interest this year because California has joined several other states that allow taxpayers to report use tax on their income tax returns. Many businesses are asking whether they should now report use tax on returns they file with the California Franchise Tax Board, rather than those they file with the Board of Equalization (BOE).

Persons and businesses that file sales and use tax returns or use tax returns (those holding a seller's permit or a certificate of registration—use tax) should continue to report their purchases subject to use tax on the tax returns they file with the Board. They may not elect to report their use tax liability on the Franchise Tax Board return. However, persons or businesses that do not file sales and use tax returns or use tax returns may elect to report their use tax liability on the Franchise Tax Board return.

What is use tax?

Use tax generally applies to the use of tangible personal property in California that has been purchased without payment of California sales tax. Use tax does not apply to property held for resale, or for property that is used only for demonstration and display while being held for sale in the regular course of business.

Use tax is calculated on the item's purchase price. The rate is the same as your sales tax rate.

When do I owe use tax?

Typically, you owe use tax on items

- Purchased for use in this state from an out-of-state retailer who does not collect California tax, or
- Purchased for resale, but withdrawn from inventory and used in this state for another purpose.

Examples

- You buy office equipment over the Internet from an out-of-state vendor who does not collect California tax. Since you will use the equipment in your business in California, you owe use tax on the purchase price.
- You operate a convenience store and purchase soda for resale without payment of California sales tax reimbursement. However, instead of selling the soda, you take five cases home for a birthday party. Since you consumed the soda instead of reselling it, you owe California use tax on the cost of the soda. Please note, if you took home *food items* for the party (for example, hot dogs, buns and chips), you



would not owe use tax because you are consuming food products that were exempt from tax when you purchased them. For those items on which you owe use tax, you should report your use tax liability by reporting the purchase price on line 2 of your tax return "Purchases Subject to Use Tax."

Note: There are some instances where donations to certain charitable organizations are not subject to tax. For more information on these types of donations, contact our Information Center.

What if I already paid use tax to my out-of-state supplier?

Some out-of-state retailers are required to, or have voluntarily registered to, collect and report California use tax from their customers. You do not need to report the purchase on line 2 of your return if you already paid the correct amount of California tax to your out-of-state supplier and that supplier is registered to collect the tax. In order to relieve your liability for the use tax, you must obtain and keep a receipt or invoice from the supplier that includes: the retailer's name, address and California seller's permit number or use tax registration number (certificate of registration—use tax); your (the purchaser's) name and

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Sales and use tax rate in the city of Point Arena will increase April 1, 2004

The sales and use tax rate in the city of Point Arena will increase to 7.75% on April 1, 2004. Voters have approved a 0.50% City of Point Arena transactions and use tax, which will increase the tax rate within the city limits from 7.25% to 7.75%.

Note: Point Arena is located in Mendocino County. The tax rate in the areas of the county outside the city of Point Arena and the city of Willits (which also has a 7.75% tax rate) will remain at 7.25%.

Who must collect tax at the new rate?

You must apply the new tax rate if you

- Are a retailer in the city of Point Arena and your merchandise is sold and delivered within the city.
- Are a retailer located outside the city of Point Arena who is engaged in business in the city and you sell merchandise for use in the city. You are considered to be engaged in business in the city if you (1) have any type of business location there, (2) deliver into the city using your own vehicles, or (3) have an agent or representative in the city for the purpose of taking orders, delivering, installing, selling, or assembling.
- Are a dealer of vehicles, vessels, or aircraft and sell those items to persons who will register or license them to an address located in the city of Point Arena.
- Collect tax on lease payments you receive for leased property used by the lessee in the city of Point Arena.

Is there an exemption from the tax rate increase?

In general, fixed-price contracts and fixed-price lease agreements entered into prior to April 1, 2004, are subject to the tax rates in effect at the time you and your customer entered into the contract or lease agreement. To qualify as “fixed-price,” neither party can have the unconditional right to adjust the price for an increase in costs or terminate the contract or lease [Revenue and Taxation Code sections 7261(g) or 7262(f)]. In addition, the tax amount or rate must be specifically stated in the contract or lease agreement. If the contract or lease qualifies as fixed-price, you should continue to report and remit the specified tax rate—that is, the rate in effect at the time you entered into the contract.

Revenue swap—I’ve seen it in the news.

What does it mean to me?

There has been a lot of media coverage about shifting taxes in order to help balance the California budget. As explained below, there are two pieces of legislation that involve shifting taxes. Under either scenario, however, the statewide tax rate will remain unchanged and the way you report your taxes—including local tax schedules—will not change.

Assembly Bill 7X. Last year, the Legislature enacted Assembly Bill 7X, which increases the state tax rate (which forms a part of the statewide 7.25% tax rate) by 0.50% but decreases the local tax rate by .50% (revenues from the state increase will be returned to local governments by use of property tax revenues). This “revenue swap” allows for the repayment of bonds issued for the Fiscal Recovery Fund.

Assembly Bill 9. In December 2003, the Legislature passed Assembly Bill 9, which, if approved by voters in March 2004, will repeal Assembly Bill 7X and instead provide for a 0.25% increase in the state rate and a decrease of 0.25% of the local tax rate. Should Assembly Bill 9 not pass, Assembly Bill 7X will go into effect.

Managed audits are back—more taxpayers are now eligible

For more information on managed audits, please see publication 53, Guide to the Managed Audit Program. —Editor

Audits are traditionally performed by auditors who visit a business location to review books and records related to sales and other transactions. However, beginning January 1, 2004, the Board will again offer a voluntary managed audit program (MAP), through which taxpayers can perform much of the audit work themselves.

A managed audit is basically a “self-audit” carried out under the direction of a Board auditor. Eligible taxpayers are provided with written and oral instructions that enable them to conduct many of the audit tasks ordinarily performed by the auditor.

You are eligible for a managed audit if you meet all of the following criteria:

- Your business transactions involve few or no statutory exemptions;
- Your business activities involve a single or small number of clearly defined taxability issues;
- You agree to participate in the MAP; and
- You have the resources to comply with the managed audit instructions provided by the Board.

Note: Previously, taxpayers who were required to make prepayments of their quarterly tax were not eligible for the managed audit program. This restriction has been eliminated in the new program.

What is the advantage to a self-managed audit?

If you complete a managed audit pursuant to the MAP Participation Agreement and owe additional tax, you will pay interest on that tax liability at only one-half the rate that would otherwise apply.

E-File your sales and use tax return with confidence!

E-filing is fast, easy, convenient, and virtually error-free. Plus, you will receive immediate confirmation that the Board of Equalization has received your return.



Benefits of E-Filing

- No preregistration required
- Mathematical calculations are performed for you
- Returns are processed in real time
- Provides the convenience of filing your return and making payments over the Internet

Who Can E-File?

You can e-file if you

- Conduct business from a single location, or
- Use BOE-401-EZ, or
- Use form BOE-401-A with schedules A and T only.

To E-File

To read about e-filing and to select a service provider, log onto our website at www.boe.ca.gov. Scroll down to “efile information” under electronic services.

Note: The service provider may charge a fee for this service. This fee is neither set by, nor shared with, the Board of Equalization.

Taking care of BUSINESS

Receive Public Agenda Notices by e-mail

www.boe.ca.gov/agenda/

To take advantage of this free service, go to the Web address above and fill out a simple request form.

You can also view Public Agenda Notices online 10 days before the meeting. Go to www.boe.ca.gov and click on “Board and Committee Meetings.”

“F.O.B. Reservation” required for exempt shipments to Indians

If a seller ships tangible personal property by mail or common carrier to an Indian purchaser on an Indian reservation and wants to claim an exemption for the sale, the sales documents must specify the delivery terms to be “F.O.B. Reservation.”

Many businesses mistakenly believe that sales of merchandise shipped to an Indian customer on an Indian reservation are automatically exempt from California sales and use tax. As explained below, certain conditions must be met for the exemption to apply.

Shipments of tangible personal property to Indian customers on Indian reservations are not taxable if all of the following conditions are met:

- The sale is to an Indian who resides on a reservation,* and
- The property is delivered to the Indian purchaser on the reservation, and
- The sale of the property to the Indian purchaser occurs *on the reservation*.

This last requirement is usually the one that causes problems for retailers. Generally, the sale will occur

- *On the reservation* when delivery to the reservation is made using the retailer’s vehicle.
- *At the seller’s shipping dock*, not on the reservation, when delivery is made by mail or other common carrier – for example, by UPS or Federal Express. When a common carrier is used, the sale generally occurs at the time the seller gives the property to the carrier.

Accordingly, sales by a California retailer will be subject to sales tax when the purchased item is shipped by mail or common carrier even though the property was shipped to an Indian customer on an Indian reservation **unless** the shipping docu-

ments show that the seller shipped the property “F.O.B. Reservation.”

Retailers should document exempt sales

Retailers should retain copies of documents that establish the customer is an Indian and resides on a reservation—such as a tribal ID card, a letter from the tribal council, or a letter from the U.S. Department of the Interior.

Retailers should also obtain an exemption certificate (this can be in the form of a letter) from the purchaser that includes the following information:

- The date,
- Name and address of the Indian purchaser,
- Documentation establishing that the Indian purchaser resides on a reservation,
- Signature of the Indian purchaser,
- Seller’s permit number of the Indian purchaser (if the purchaser does not hold a seller’s permit, the certificate should explain why),
- A description of the property purchased under the certificate, and
- A statement explaining why the sales tax does not apply.

Note: As explained above, the sale is subject to tax if the sale is made to the Indian purchaser off the reservation. If the property is delivered by mail or common carrier, the sale is subject to tax unless shipment is made “F.O.B. Reservation.”

For more information about how tax applies to sales to Indians, see Regulation 1616, *Federal Areas*.

* For purposes of the Sales and Use Tax Law, *Indian* means any person of Indian descent who is entitled to receive services from the U.S. Department of Interior. Indian

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We recommend that you get tax advice in writing

For your protection, it is best to get tax advice in writing.



You may be relieved of tax, penalty, and interest charges if the Board determines you reasonably relied on written advice from us and in reliance on that advice, you did not charge or collect sales tax reimbursement or use tax from your customer or pay use tax on your storage or use of property you purchased.

For relief to apply, you must give us a written request for advice that identifies you and fully describes the specific facts and circumstances of the activities or transaction for which the advice is requested. In describing the specific facts of a transaction, it would be helpful if you included in your letter copies of representative documents for your business transactions, such as sales contracts, purchase orders, and invoices.

Note: This relief is not available for advice given over the telephone or in person. Relief also does not apply if you rely on written advice that is given to a different person, even if your transactions are similar. Occasionally, you may receive a copy of a Board letter from a supplier or business associate, explaining that a transaction is exempt from tax. Since you have transactions comparable to those in the letter, you rely on that letter to report tax. If the advice in the letter is incorrect, you are not eligible for relief because the advice was not provided to you by the Board based on your *own* inquiry.

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organizations are entitled to the same exemptions as are individual Indians. Indian organizations include Indian tribes, tribal organizations and partnerships all of whose members are Indians. The term also includes corporations organized under tribal authority and wholly owned by Indians. Other corporations, including those wholly owned by Indians, are excluded from the term. "Reservation" includes reservations, rancherias, and any land held by the United States in trust for any Indian tribe or individual Indian.

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address; the date of sale; a description of the property sold; the sale amount and the amount of the tax paid. For more information on use tax, please order publications 110, *California Use Tax Basics* and 112, *Purchases from Out-of-State Vendors*.

New or revised reference material

Sales and Use Tax Publications

- 52 Vehicles and Vessels: How to Request a Use Tax Clearance for DMV Registration (November 2003)
- 57 Innocent Spouse Relief from Sales and Use Tax (October 2003)
- 71 California City and County Sales and Use Tax Rates (October 2003) (insert added to note tax rate increase in Point Arena on April 1, 2004)
- 102 Sales to the U.S. Government (October 2003)

Sales and Use Tax Regulations (New)

- 1620.1 Sales of Certain Vehicles & Trailers for Use in Interstate or Out-of-State Commerce (effective October 16, 2003)

Sales and Use Tax Regulations (Revised)

- 1630 Packers, Loaders and Shippers (effective October 15, 2003)
- 1802 Place of Sale and Use for Purposes of Bradley Burns Uniform Local Sales and Use Taxes (effective November 28, 2003)

Translated Publications

C = Chinese • K = Korean • S = Spanish • V = Vietnamese

- 42-S Resale Certificate Tips (July 2002)
- 51-K,S Guide to Board of Equalization Services (April 2003)
- 70-C,K,S,V The California Taxpayer's Bill of Rights (April 2003)
- 71-C,S California City and County Sales and Use Tax Rates (October 2003)
- 73-K,S California Seller's Permit (March 2003)
- 102-S Sales to the U.S. Government (September 2002)

For More Information All telephone numbers are toll-free.

Internet	www.boe.ca.gov ■ www.taxes.ca.gov
Information Center	800-400-7115 Telephone devices for the deaf 800-735-2929 (TDD) ■ 800-735-2922 (Voice)
Requests for Fax Copies	800-400-7115 (Choose automated services.)
Seller's Permit Verification	888-225-5263 ■ www.boe.ca.gov
Taxpayers' Rights Advocate	888-324-2798 ■ www.boe.ca.gov
Tax Evasion Hotline	888-334-3300
State Legislation	www.leginfo.ca.gov