



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

DRAFT

Date:	05/14/13	Bill No:	<a href="#">Senate Bill 688</a>
Tax Program:	Sales and Use	Author:	Galgiani
Sponsor:	BOE	Code Sections:	RTC 6018.1, 6358.3
Related Bills:		Effective Date:	First day of the first calendar quarter commencing more than 90 days after enactment

**BILL SUMMARY**

Until January 1, 2018, this bill exempts from the sales and use tax the use, furnishing, or sale of drugs and medicines for the treatment of animals by: (1) a licensed veterinarian, (2) a city, city and county, county, or other local government animal shelter, or (3) a nonprofit animal welfare or rescue organization.

**Summary of Amendments**

Since the previous analysis, this bill was amended to add a January 1, 2018 sunset date and to require the Legislative Analyst’s Office (LAO) to conduct a study as described.

**ANALYSIS**

**CURRENT LAW**

Except where specifically exempted by statute, California’s Sales and Use Tax Law<sup>1</sup> imposes the sales tax on all retailers for the privilege of selling tangible personal property at retail in this state or the use tax on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer.

Generally, persons engaged in the business of selling tangible personal property must obtain a seller’s permit. These persons must also report the tax on a Board of Equalization (BOE)-prescribed return. However, under various statutes, some smaller or service-based businesses and certain nonprofit organizations that make certain types of sales are regarded as consumers and not sellers. These entities are referred to as a “statutory consumers.” Qualifying sales by a statutory consumer are not considered retail sales. Therefore, a statutory consumer need not report or pay tax on his or her sales or obtain a seller’s permit (unless he or she makes other non-qualifying retail sales). Rather, tax generally is owed on the sale to the statutory consumer of the products intended for resale to the statutory consumer’s customer.

Under existing law,<sup>2</sup> licensed veterinarians are considered statutory consumers of drugs or medicines, as defined, used or furnished when they perform professional services. Under this provision, as consumers, licensed veterinarians pay sales tax reimbursement to their suppliers or use tax on purchases of drugs and medicines they use or furnish when they perform their professional services.

<sup>1</sup> Part 1 (commencing with Section 6001) of Division 2 of the Revenue and Taxation Code (RTC).

<sup>2</sup> RTC Section 6018.1.

*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 BOE’s formal position.*

For food animals, such as cows, chickens, and pigs, existing law exempts sales and purchases of drugs and medicines administered directly to the animals<sup>3</sup> or as an additive to feed or drinking water<sup>4</sup> when the drug's or medicine's primary purpose is to prevent or control disease. Also, Section 6358.4 exempts sales and purchases of drugs and medicines administered to nonfood animals as an additive to feed or drinking water when the animal or its offspring is to be sold in the regular course of business. Therefore, a licensed veterinarian's drug and medicine purchases and subsequent sales are exempt from the sales and use tax when he or she administers them directly to the animals or as an additive to feed or drinking water to prevent or control disease.

Existing law<sup>5</sup> requires animal shelters and animal rescue organizations to report and pay sales tax on their drug and medicine sales, unless those sales are made in connection with a pet adoption. For sales made in connection with a pet adoption, such as vaccinations, existing law requires these organizations either to pay sales tax reimbursement or use tax on their purchases of drugs and medicines they use in connection with those services.

California law<sup>6</sup> provides for the regulation of veterinary medicine practices. Absent the required license from the California Veterinary Board, the law prohibits persons from the practice of veterinary medicine.

#### PROPOSED LAW

Until January 1, 2018, this bill suspends the "statutory consumer" provision related to licensed veterinarians. Instead, this bill creates a sales and use tax exemption until January 1, 2018, for drugs and medicines used, furnished, or sold for the treatment of animals by:

- A licensed veterinarian,
- A city, city and county, county, or other local government animal shelter, or
- A nonprofit animal welfare or rescue organization.

The bill defines "animal," "drugs and medicines," "licensed veterinarian," and "nonprofit animal welfare or rescue organization."

The bill also requires the LAO to conduct a study, with BOE-provided information, that measures the exemption's effect on Internet veterinary medicine purchases, veterinary medicine costs to consumers, and the aggregate number of veterinary visits. The bill requires the LAO to submit the study to specific legislative committees.

#### COMMENTS

1. **Sponsor and purpose.** Upon unanimous vote of its members, the BOE is sponsoring this bill in an effort to enable California veterinarians to reduce medical costs and improve pet health. The BOE believes that medication provided by a licensed veterinarian offers more quality assurance than medication obtained elsewhere. Other outlets often are not well regulated and may not remit California sales tax. Exempting drugs and medicines sold by licensed veterinarians, local animal shelters, and animal welfare and rescue organizations will reduce the cost of

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<sup>3</sup> RTC Section 6358.

<sup>4</sup> RTC Section 6358.4.

<sup>5</sup> RTC Section 6010.40.

<sup>6</sup> Chapter 11 (commencing with Section 4800) of Division 2 of the Business and Professions Code.

purchasing medication under a veterinarian's supervision, and will discourage consumers from going to other outlets to purchase medicine for their pets.

2. **The May 14, 2013 amendments** add a January 1, 2018 sunset date and require the LAO to conduct a study, as described, with BOE-provided information, and submit the study to specified Legislative committees
3. **Most veterinarians likely are registered with the BOE.** Although currently, veterinarians need not register with the BOE to sell drugs and medicines used or furnished in the course of their professional services, most are likely registered as retailers. Many veterinarians sell pet supplies or other products besides drugs and medicines. These veterinarians are required to hold a BOE-issued seller's permit and file returns with the BOE to report and pay the tax. Also, existing law<sup>7</sup> requires a "qualified purchaser" to register with the BOE and annually report and pay use tax to the BOE. A "qualified purchaser" includes businesses without seller's permits that have at least \$100,000 in annual gross receipts from business operations. Those veterinarians that are not required to hold seller's permits that meet the required gross receipts also may be registered with the BOE to report use tax as a "qualified purchaser."
4. **BOE would not have the LAO study information.** By January 1, 2017, the bill requires the LAO, with BOE-provided information, to study the exemption's effect on Internet veterinary medicine purchases, veterinary medicine costs to consumers, and the aggregate number of veterinary visits.

The BOE would not have any data related to these effects, as none of this information is reported to the BOE currently. Also, since this bill proposes a complete state and local tax exemption, veterinarians, shelters, and rescue organizations making qualifying exempt sales may not provide sufficient information on their returns to enable the BOE to even determine the dollar amount of exemptions claimed. To address this issue, we suggest the bill require the BOE to provide any information available in its records. The suggested amendment is shown as Amendment 2 on page 5 of this analysis.

5. **Exemption does not materially affect tax administration.** The bill's drug and medicine definition is the same as that used in current Section 6018.1 that identifies licensed veterinarians as statutory consumers. The BOE has administered that provision since 1985, and we do not anticipate any administrative concerns related to this bill's proposed exemption.
6. **Technical amendment.** On page 3, proposed Section 6018.1(b) needs a technical correction to refer to the operative date of the subdivision, rather than the operative date of the section. Amendment 1 on Page 5 shows the suggested amendment.

## COST ESTIMATE

If enacted, the BOE will incur absorbable costs to notify taxpayers, and respond to taxpayer, media, and public inquiries.

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<sup>7</sup> RTC Section 6225.

**REVENUE ESTIMATE****BACKGROUND, METHODOLOGY, AND ASSUMPTIONS**

According to the American Pet Products Association, U.S. consumers spent an estimated \$13.6 billion on veterinary care in 2012. Based on California's 12% share of U.S. population, we estimate that California consumers will spend about \$1.63 billion ( $12\% \times \$13.6 \text{ billion} = \$1.63 \text{ billion}$ ) on veterinary care.

We have no industry or census data that discloses specific information about licensed veterinarians' drug and medicine purchases. According to one industry study, veterinarian clinic expenditures of an estimated 15% ( $15\% \times \$1.63 \text{ billion} = \$244.6 \text{ million}$ ) is attributable to purchases of goods and services, such as medicine and diagnostic tests.

As an order of magnitude, if we assume that 50% of all purchases are attributable to drugs and medicines described in the bill, then purchases exempted by this measure amount to an estimated \$122.3 million annually ( $50\% \times \$244.6 \text{ million} = \$122.3 \text{ million}$ ).

We do not have specific data attributable to drugs and medicines used, furnished or sold by local animal shelters or animal welfare organizations.

**REVENUE SUMMARY**

The annual sales and use tax revenue loss from exempting drugs and medicine used, furnished, or sold by licensed veterinarians amounts to \$10.2 million ( $\$122.3 \times 8.38\% = \$10.2 \text{ million}$ ).

Revenue Source	Rates	(in millions)
State General Fund	3.94%	\$4.8
State Education Protection	0.25%	0.3
Fiscal Recovery Fund	0.25%	0.3
Local Revenue Fund	0.50%	0.6
Local Public Safety Fund	0.50%	0.6
Local Revenue Fund 2011	1.06%	1.3
Bradley Burns (Local Tax)	1.00%	1.2
Special District Tax <sup>8</sup>	0.88%	1.1
Total State and Local Revenue Loss	8.38%	\$10.2

This revenue estimate does not account for any changes in economic activity that may or may not result from enactment of the proposed law.

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<sup>8</sup> This is the average tax rate imposed by special districts in California.

STATE BOARD OF EQUALIZATION  
PROPOSED AMENDMENTS TO SB 688

Amendment 1

On page 3, line 18, substitute “subdivision” for “section” after “act adding this”

Amendment 2

On page 4, line 12, strike the comma after “board” and add “*available in the board’s records*” after “by the board”