



Date Amended:	04/14/09	Bill No:	<u>AB 711</u>
Tax:	Use Tax	Author:	Calderon
Related Bills:	AB 469 (Eng) AB 819 (Calderon)		

BILL SUMMARY

This bill would require a qualified purchaser, as defined, to register with the Board and report and pay by April 15, the use tax owed for the previous calendar year.

ANALYSIS

CURRENT LAW

Under existing law, Chapter 3 (commencing with Section 6201) of Part 1 of Division 2 of the Revenue and Taxation Code imposes a use tax on the storage, use, or other consumption in this state of tangible personal property purchased from any retailer. The use tax is imposed on the purchaser, and unless that purchaser pays the use tax to a retailer registered to collect the California use tax, the purchaser is liable for the tax, unless the use of that property is specifically exempted or excluded from tax. The use tax is the same rate as the sales tax and is required to be remitted to the Board on or before the last day of the month following the quarterly period in which the purchase was made, or on the purchaser's state income tax return filed with the Franchise Tax Board. Generally, a use tax liability occurs when a California consumer or business purchases tangible items for their own use from an out-of-state retailer that is not registered with the Board to collect the California use tax.

PROPOSED LAW

This bill would add Section 6225 to the Revenue and Taxation Code to require "qualified purchasers" to register with the Board and report and pay by April 15, the use tax owed for purchases made during the calendar year. The bill would define "qualified purchaser" as a person that meets all of the following conditions:

- (1) The person is required to hold a business license as required by the local ordinance of the city, county, or city and county in which the person conducts business.
- (2) The person is not required to hold a seller's permit pursuant to this part.
- (3) The person is not required to be registered pursuant to Section 6226.
- (4) The person is not a holder of a use tax direct payment permit as described in Section 7051.3.

The bill would state that it is the intent of the Legislature that the revenues deposited into the General Fund be annually appropriated to the Intellectual Property Piracy Prevention and Prosecution Fund.

The bill would become operative only if AB 819 (Calderon) is also enacted.

IN GENERAL

In 1933, California enacted its first retail sales tax. Within a few years of the adoption of the sales tax, California retailers believed they were facing unfavorable competition from retailers in states that had not adopted a sales tax. Customers could choose to go to a neighboring state without a sales tax and avoid paying the tax on their purchases. California responded to this challenge in 1935 by adopting a use tax. The use tax is virtually identical to the sales tax, except it is imposed on the storage, use or consumption of the goods; and the tax is imposed on the sales price of the good. The intent of a use tax is to offset the incentive to purchase from retailers in other states with low sales tax rates or no sales tax.

Although the use tax is now imposed by every state that has a sales tax, there has been limited success in collecting the use tax. Unlike the retail sales tax which requires in-state retailers to collect the tax, states have been unable to impose a similar compliance and collection requirement on out-of-state retailers (an out-of-state retailer is required to have physical presence in a state in order to require that retailer to collect the use tax).

Therefore, California must rely on purchasers to report their use tax obligations on their out-of-state purchases, such as those made over the Internet or through mail order. And, even though a separate line is currently on the state income tax return with accompanying instructions in the booklet for use tax reporting, the compliance rate remains very low. Unreported use tax is the largest area of noncompliance in California's sales and use tax program - an estimated \$1.2 billion annually is attributable to unreported California use tax by both businesses and individual consumers. For 2008, the Franchise Tax Board processed over 18.5 million returns, yet only 44,114 state income tax returns had use tax reported, yielding only \$9 million in state and local use tax revenues.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author in order to provide a funding source through the enhanced collections of use tax to ensure that local law enforcement and district attorneys are equipped with the necessary funding for personnel and equipment necessary to successfully interdict the promulgation of high technology crime.
2. **Entities that would be affected.** Enactment of this bill would essentially apply to all businesses that are not already registered with the Board. We anticipate approximately 2 million businesses would fall under this measure's parameters.
3. **Additional lead time would be necessary.** Enactment of this bill would significantly impact the Board's operations. In order for the Board to have sufficient time to properly identify, notify, register, and educate all 2 million businesses, and hire, house, and train the additional staff required to implement and administer this bill, we suggest that the bill have a delayed operative date, preferably July 1, 2010.

4. **Bill will only become operative if another measure is enacted.** The provisions of this bill will not become operative unless another measure – AB 819 (Calderon) – becomes law. AB 819 would establish the Intellectual Property Piracy Prevention and Prosecution Program to fund grants for local law enforcement and district attorneys for purposes of preventing and prosecuting intellectual property piracy. It also contains provisions that specify that it will not become operative unless AB 711 is enacted.
5. **Related Legislation.** AB 469 (Eng), sponsored by the Board, would *require* consumers (including businesses not already registered with the Board, such as those affected by this measure) who have failed to report use tax to the Board on their taxable purchases for the preceding year to report the use tax on the income tax returns for the taxable year in which the liability for the qualified use tax was incurred, as specified.

COST ESTIMATE

Significant costs would be incurred if this bill were enacted to identify, notify, and register all affected businesses, and to process an approximate 2 million additional returns annually. An estimate of the Board’s costs is pending, however, preliminarily, we expect the costs could be at a minimum in the tens of millions.

REVENUE ESTIMATE

We estimate the fiscal year 2009-10 average statewide state and local sales and use tax rate to be 9.00 percent. This rate reflects the temporary 1 percent increase in the state rate as specified in ABX3 3, which took effect April 1, 2009. This rate also reflects the results of recent elections, in which voters in some localities approved higher transit district tax rates.

Applying this 9.00 percent rate to our 2007 estimates of purchases made with unpaid use taxes by California businesses, an estimated \$775 million annually is attributable to unpaid use tax by businesses. These unreported revenues are spread among more than two million businesses. The use tax compliance rate by retailers currently registered with the Board is about 80%. If we assume the same level of compliance would be achieved by these businesses, we could expect to gain an approximate \$620 million annually in state and local use tax revenues.

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