SENATE BILL No. 18

Introduced by Senator Steinberg

April 21, 2010

An act to amend Section 25128.5 of, and to add Section 6377 to, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

legislative counsel's digest

SB 18, as introduced, Steinberg. Sales and use taxes: exemption: manufacturing equipment: corporate income tax: single sales factor.

The Sales and Use Tax Law imposes a tax on retailers measured by the gross receipts from the sale of tangible personal property sold at retail in this state, or on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer for storage, use, or other consumption in this state. That law provides various exemptions from those taxes.

This bill would exempt from those taxes, on or after July 1, 2011, the gross receipts from the sale of, and the storage, use, or other consumption of, tangible personal property purchased by a qualified person, as defined, for use in the manufacturing process, as specified, and tangible personal property purchased for use by a contractor to perform a construction contract for a qualified person, for specified purposes.

The Bradley-Burns Uniform Local Sales and Use Tax Law authorizes counties and cities to impose local sales and use taxes in conformity with the Sales and Use Tax Law, and existing law authorizes districts, as specified, to impose transactions and use taxes in conformity with the Transactions and Use Tax Law, which conforms to the Sales and

Use Tax Law. Exemptions from state sales and use taxes are incorporated into these laws.

This bill would specify that this exemption does not apply to local sales and use taxes, transactions and use taxes, and specified state taxes.

The Corporation Tax Law imposes taxes measured by income and, in the case of a business with income derived from or attributable to sources both within and without this state, apportions the income between this state and other states and foreign countries in accordance with a specified 4-factor formula based on the property, payroll, and sales within and without this state, except that in the case of an apportioning trade or business that derives more than 50% of its gross business receipts from conducting one or more qualified business activities, as defined, business income is apportioned in accordance with a specified 3-factor formula. Existing law, for taxable years beginning on or after January 1, 2011, allows a taxpayer to make an annual election to have that income apportioned in accordance with a single sales factor formula, except as provided.

This bill would, for a taxpayer that would otherwise be able to elect to have its income apportioned in accordance with a single sales factor formula, require the taxpayer to apportion its income in accordance with a single sales factor formula.

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 6377 is added to the Revenue and Taxation Code, to read:

6377. (a) (1) On or after July 1, 2011, there are exempted from the taxes imposed by this part the gross receipts from the sale of, and the storage, use, or other consumption in this state of, any of the following:

(A) Tangible personal property purchased for use by a qualified person to be used primarily in any stage of the manufacturing, processing, refining, fabricating, or recycling of property, beginning at the point any raw materials are received by the qualified person and introduced into the process and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling has altered property to its completed form, including packaging, if required.

(B) Tangible personal property purchased for use by a contractor for use in the performance of a construction contract for the qualified person who will use the property as an integral part of the manufacturing, processing, refining, fabricating, or recycling process, or as a storage facility for use in connection with the manufacturing process.

(2) This exemption shall not apply to the sale of, or the storage, use, or other consumption of, tangible personal property that is purchased to be used primarily in administration, general management, or marketing.

(b) For purposes of this section:

(1) "Fabricating" means to make, build, create, produce, or assemble components or property to work in a new or different manner.

(2) "Manufacturing" means the activity of converting or conditioning property by changing the form, composition, quality, or character of the property for ultimate sale at retail or use in the manufacturing of a product to be ultimately sold at retail. Manufacturing includes any improvements to tangible personal property that result in a greater service life or greater functionality than that of the original property.

(3) "Primarily" means tangible personal property used 50 percent or more of the time in an activity described in subdivision (a).

(4) "Process" means the period beginning at the point at which any raw materials are received by the qualified taxpayer and introduced into the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer and ending at the point at which the manufacturing, processing, refining, fabricating, or recycling activity of the qualified taxpayer has altered tangible personal property to its completed form, including packaging, if required. Raw materials shall be considered to have been introduced into the process when the raw materials are stored on the same premises where the qualified taxpayer's manufacturing, processing, refining, or recycling activity is conducted. Raw materials that are stored on premises other than where the qualified taxpayer's manufacturing, processing, refining, fabricating, or recycling activity is conducted, shall not be considered to have

been introduced into the manufacturing, processing, refining, fabricating, or recycling process.

(5) "Processing" means the physical application of the materials and labor necessary to modify or change the characteristics of property.

(6) "Qualified person" means any of the following:

(A) A person who is engaged in those lines of business described in Codes 3111 to 3399, inclusive, or 5112 of the North American Industry Classification System (NAICS) published by the United States Office of Management and Budget (OMB), 2007 edition.

(B) An affiliate of a person qualified pursuant to subparagraph (A) shall also be considered a qualified person as long as the affiliate is included as a member of that person's unitary group for which a combined report is required to be filed under Article 1 (commencing with Section 25101) of Chapter 17.

(7) "Refining" means the process of converting a natural resource to an intermediate or finished product.

(8) "Tangible personal property" includes, but is not limited to, all of the following:

(A) Machinery and equipment, including component parts and contrivances such as belts, shafts, moving parts, and operating structures.

(B) All equipment or devices used or required to operate, control, regulate, or maintain the machinery, including, without limitation, computers, data processing equipment, and computer software, together with all repair and replacement parts with a useful life of one or more years therefor, whether purchased separately or in conjunction with a complete machine and regardless of whether the machine or component parts are assembled by the taxpayer or another party.

(C) Property used in pollution control that meets standards established by this state or any local or regional governmental agency within this state.

(D) Special purpose buildings and foundations used as an integral part of the manufacturing, processing, refining, or fabricating process, or that constitute a research or storage facility used during the manufacturing process. Buildings used solely for warehousing purposes after completion of the manufacturing process are not included.

(E) Fuels used or consumed in the manufacturing process.

(9) “Tangible personal property” shall not include any of the following:

(A) Consumables with a normal useful life of less than one year, except as provided in subparagraph (E) of paragraph (8).

(B) Furniture, inventory, and equipment used in the extraction process, or equipment used to store finished products that have completed the manufacturing process.

(c) No exemption shall be allowed under this section unless the purchaser furnishes the retailer with an exemption certificate, completed in accordance with any instructions or regulations as the board may prescribe, and the retailer subsequently furnishes the board with a copy of the exemption certificate. The exemption certificate shall contain the sales price of the machinery or equipment whose sale of, or storage, use, or other consumption is exempt pursuant to subdivision (a).

(d) (1) Notwithstanding subdivision (a), the exemption established by this section shall not apply with respect to any tax levied pursuant to Sections 6051.2, 6051.5, 6201.2, or 6201.5, or pursuant to Section 35 of Article XIII of the California Constitution.

(2) Notwithstanding any provision of the Bradley-Burns Uniform Local Sales and Use Tax Law (Part 1.5 (commencing with Section 7200)) or the Transactions and Use Tax Law (Part 1.6 (commencing with Section 7251)), the exemption established by this section shall not apply with respect to any tax levied by a county, city, or district pursuant to, or in accordance with, either of those laws.

(e) Notwithstanding subdivision (a), the exemption provided by this section shall not apply to any sale or use of property which, within one year from the date of purchase, is removed from California, converted from an exempt use under subdivision (a) to some other use not qualifying for the exemption, or used in a manner not qualifying for the exemption.

(f) If a purchaser certifies in writing to the seller that the property purchased without payment of the tax will be used in a manner entitling the seller to regard the gross receipts from the sale as exempt from the sales tax, and within one year from the date of purchase, the purchaser (1) removes that property outside California, (2) converts that property for use in a manner not qualifying for the exemption, or (3) uses that property in a manner not qualifying for the exemption, the purchaser shall be liable for payment of sales tax, with applicable interest, as if the purchaser were a retailer making a retail sale of the property at the time the property is so removed, converted, or used, and the sales price of the property to the purchaser shall be deemed the gross receipts from that retail sale.

SEC. 2. Section 25128.5 of the Revenue and Taxation Code is amended to read:

25128.5. (a) Notwithstanding Section 38006, for taxable years beginning on or after January 1, 2011, any apportioning trade or business, other than an apportioning trade or business described in subdivision (b) of Section 25128~~, may make an irrevocable annual election on an original timely filed return, in the manner and form prescribed by the Franchise Tax Board to~~ *shall* apportion its income in accordance with this section, and not in accordance with Section 25128.

(b) Notwithstanding Section 38006, for taxable years beginning on or after January 1, 2011, all business income of an apportioning trade or business ~~making an election~~ described in subdivision (a) shall be apportioned to this state by multiplying the business income by the sales factor.

(c) The Franchise Tax Board is authorized to issue regulations necessary or appropriate regarding the ~~making of an election under~~ *administration of* this section~~, including regulations that are consistent with rules prescribed for making an election under Section 25113~~.

SEC. 3. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.

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