

# Client Alert

October 14, 2015

## California Governor Signs Bill Limiting Cities and Counties Use of Sales/Use Tax Agreements

By Eric J. Coffill

The governor of California has signed SB 533, which, beginning on January 1, 2016, further limits the power of a city or a county to enter into an agreement with a retailer that would result in the payment, transfer, diversion, or rebate of local sales and use tax.

On October 9, 2015, Governor Brown signed Senate Bill 533 (Ting), Stats. 2015, c. 717, which generally prohibits a California local agency on or after January 1, 2016, from entering into an agreement that would result in the payment, transfer, diversion, or rebate of Bradley-Burns local tax proceeds to a retailer if the agreement results in a reduction of revenue that is received by another local agency.

Under current law, the Bradley-Burns Uniform Local Sales and Use Tax Law authorizes counties and cities to impose a local sales and use tax of up to 1% on tangible personal property sold at retail in the city/county or purchased outside the city/county for use in the city/county.<sup>1</sup> All cities and counties in California impose Bradley-Burns local taxes at the uniform rate of 1%.<sup>2</sup> As a consequence, local officials often engage in competition involving sales taxes which are assigned by place of sale.<sup>3</sup> For example, a county or city can offer a sales tax rebate to a business that consolidates all of its California sales into that county or city by opening a buying company in that jurisdiction.<sup>4</sup> In the words of the bill's author, "It is becoming increasingly common practice for companies to pressure local agencies to provide a sales tax revenue rebate on the promise to book all sales from multiple sales with that local agency."<sup>5</sup> The bill's author argues that "when the sales tax revenue from commercial activity in one jurisdiction is booked in another, the local agency that is losing the sales tax revenue must continue

<sup>1</sup> Cal. Rev. & Tax. Code section 7200 *et seq.* The statewide tax rate is 7.5%, which includes this 1% local city/county tax. In most areas of California, local jurisdictions also have added district taxes that increase the tax owed by a seller. Those district tax rates range from 0.10% to 2.00%. Some areas may have more than one district tax in effect. Sellers are required to report and pay the applicable district taxes for their taxable sales and purchases. See California State Board of Equalization, "California City & County Sales and Use Tax Rates," <http://www.boe.ca.gov/sutax/pam71.htm>.

<sup>2</sup> Of the 1%, cities and counties use 0.75% to support general operations. The remaining 0.25% is designated by statute for county transportation purposes and is restricted to road maintenance or the operation of transit systems. Counties receive the 0.25% tax for transportation purposes regardless of whether the sale occurs in a city or in the unincorporated area of a county. See Assembly Committee on Revenue and Taxation, SB 533 Bill Analysis, Date of Hearing July 13, 2015, p. 1.

<sup>3</sup> "Place of sale" for purpose of the local sales tax is defined by Revenue and Taxation Code section 7205 as the place of business of the retailer. If the retailer has only one place of business in California, all California retail sales in which that place of business participates occur at that place of business. The California State Board of Equalization allocates the local sales tax to the city, county, or city and county in which that place or business is located, even if title to the property passes to the purchaser outside the jurisdiction in which the retailers business is located or if the property is never within the jurisdiction in which the retailer's business is located. If the retailer has more than one place of business in California, Board of Equalization Regulation 1802(a)(2)(b) provides the place of sale is where principal negotiations are carried on. See California State Board of Equalization, Legislative Bill Analysis, SB 533, June 10, 2015, p. 1.

<sup>4</sup> Senate Rules Committee, SB 533 Bill Analysis, Aug. 31, 2015, p. 6.

<sup>5</sup> Office of Senator Richard Pan, SB 533 Fact Sheet, Updated 10/2/2015, p. 1.

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to provide police and fire protection services to the company since it maintain a physical presence within the territory of the local agency, and the local agency streets and other services are used and must be maintained.”<sup>6</sup>

Current law prohibits a local agency, as defined to mean all cities and counties, from entering into an agreement that would involve any such rebate of the Bradley-Burns local tax if the agreement results in a reduction in the amount of revenue that is received by another local agency from a retailer that is located within another local agency, and the retailer continues to maintain a physical presence within the jurisdiction of that other agency.<sup>7</sup> However, there are a number of specified exceptions under current law, one being an exception for an agreement to pay or rebate any Bradley-Burns local tax revenue relating to a buying company, by which companies are consolidating statewide sales all in one location.<sup>8</sup> Another exception is where a retailer expands its operations into another jurisdiction with the result that retailer is conducting comparable operations within the jurisdiction of both agencies.<sup>9</sup>

SB 533 repeals both these exceptions under current law and provides that beginning on or after January 1, 2016, a local agency is prohibited from entering into any form of agreement that would result in the payment, transfer, diversion, or rebate of any amount of Bradley-Burns local tax proceeds to any person for any purpose when (1) the agreement results in a reduction in the amount of such proceeds that, in the absence of the agreement, would be received by another local agency, and (2) the retailer continues to maintain a physical presence within the territorial jurisdiction of that other local agency, with specified limited exemptions.<sup>10</sup> Where an agreement is not prohibited by this section, the agency is required to post online any new agreement, as well as agreements entered into prior to January 1, 2016 (i.e., the effective date of SB 533), that are still in effect on or after that date which result in a reduction of the amount of Bradley-Burns local tax proceeds that, in the absence of the agreement, would be received by another local agency. In addition, an agency entering into a new agreement must notify the other local agency by certified mail at least 60 days prior to ratification or approval of that agreement.

The Board of Equalization bill analysis noted the purpose of SB 533 was to “prohibit cities and counties from using Bradley-Burns sales tax rebates as an incentive to draw sales tax-generating activity away from other communities.”<sup>11</sup> The bill was supported by a number of cities, as well as the League of California Cities. The City of West Sacramento, a vocal supporter and sponsor of the bill to prevent a “race to the bottom” among municipalities competing for revenues,<sup>12</sup> argued there are “fiscally predatory jurisdictions and a growing cottage industry of consultants dedicated to helping them still seek loopholes...” under the current law, with the current

<sup>6</sup> Office of Senator Richard Pan, SB 533 Fact Sheet, Updated 10/2/2015, p. 1.

<sup>7</sup> Government Code section 53084.5. See SB 533, Legislative Counsel's Digest.

<sup>8</sup> Government Code section 53084.5 Senate Rules Committee, SB 533 Bill Analysis, Aug. 31, 2015, p. 6.

<sup>9</sup> Government Code section 53084.5.

<sup>10</sup> An agreement would be allowed to pay or rebate any use tax revenue related to a use tax direct payment permit issued under Revenue and Taxation Code section 7051.3. An agreement also would be allowed for a mutual tax revenue sharing agreement between local agencies to pay, transfer, or divert Bradley-Burns tax revenue where the agreement would not result in the payment, transfer, diversion, or rebate of those tax revenues to a retailer.

<sup>11</sup> California State Board of Equalization, Legislative Bill Analysis, SB 533, June 10, 2015, p. 1.

<sup>12</sup> Assembly Committee on Revenue and Taxation, SB 533 Bill Analysis, Date of Hearing July 13, 2015, p. M. See Office of Senator Richard Pan, SB 533 Fact Sheet, Updated 10/2/2015, p. 2. Senator Pan's Senate District 6 includes West Sacramento.

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statutory exception for having comparable operations with the jurisdiction of both agencies being “an essentially meaningless qualifier that mostly serves to facilitate the very types of agreements the law is intended to preclude.”<sup>13</sup> The City of West Sacramento disclosed that it recently had seen its sales tax revenue from a local business drop by over \$1 million annually as a result of a deal between that business and a distant jurisdiction, even though the business continues to operate in West Sacramento.<sup>14</sup> On the other side of the issue, the County of San Bernardino went on record as opposing the bill and argued that business owners who are prohibited from receiving economic incentives to expand operations outside of the original jurisdiction to other areas instead may choose to completely close down operations or move their business to a new location which may be outside California. The County of San Bernardino argued the bill “prohibits normal incentives, designed to encourage local businesses to expand and upgrade, so they can generate additional tax revenue and jobs for the local community.”<sup>15</sup>

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<sup>13</sup> Senate Rules Committee, SB 533 Bill Analysis, Aug. 31, 2015, p. 7.

<sup>14</sup> Assembly Committee on Revenue and Taxation, SB 533 Bill Analysis, Date of Hearing July 13, 2015, pp. F-G.

<sup>15</sup> Senate Rules Committee, SB 533 Bill Analysis, Aug. 31, 2015, pp. 7-8.