



May 4, 2007

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The Honorable Betty Yee, Chair  
The Honorable Judy Chu, Vice Chair  
The Honorable Michelle Steel, Member  
The Honorable Bill Leonard, Member  
The Honorable John Chiang, State Controller and Member  
State Board of Equalization  
450 N Street  
P.O. Box 942879  
Sacramento, CA 94279

Re: Reallocation and Recharacterization of Use Tax Revenues; Proposed Changes to Regulations 1802 and 1803

Dear Chair and Board Members:

On behalf of the California State Association of Counties (CSAC), I respectfully submit our opposition to the changes proposed to Regulation 1803, and the conforming change proposed to Regulation 1802. I also submit our neutrality on the other proposed change to Regulation 1802. There are many reasons that you should cast your vote against this proposal, which fall into the following three categories: arguments from statute, arguments from history, and arguments from policy.

First, and most importantly, is the argument from statute. California Revenue and Taxation Code Sections 7202 (b), relating to the local sales tax, and 7203 (a), relating to the local use tax, require in part that local agencies that opt into the "Bradley-Burns Uniform Local Sales and Use Tax" include in their implementing ordinance "provisions identical to those" that govern the state's sales and use tax laws. They also require a provision that "all amendments [to the state codes]...shall automatically become a part of the sales tax ordinance of the county." These code sections make it exceedingly clear that local agencies that have chosen to participate in the Bradley-Burns system – and all cities and counties have made that choice – agree that *the characterization of their local sales and use taxes will exactly mirror those of the state*. The proposal under consideration would subvert that requirement by having some transactions characterized as a state use tax but a local sales tax. This would not only be confusing for persons doing business in this state, but would directly contradict California law. The Board of Equalization's tax regulations exist to carry out and clarify statutes, and cannot contradict or undermine them. This proposed change brings before the Board primarily a legal question, so the Board must primarily look to the law for the answer. Therefore, on this basis alone, the Board must reject the proposed change.

Second is the argument from history. The staff documentation on this point – in which they show that the historical interpretation of law by the Board is consistent with current practice – is careful, extensive, and persuasive, so we will not dwell on it here at much length, except to rebut the presumption by the proponent that cities would not have chosen to join the Bradley-Burns system if it meant they could not collect sales tax (as opposed to use tax) on the transactions under consideration here. On the contrary, we would submit that the reason every city and county has chosen to have the Board of Equalization administer their local taxes under a uniform system is because the efficiencies are so great that even if they lost a minor amount of revenue by this difference in characterization of sales versus use tax, they gained far more revenue by not having to run their own system.

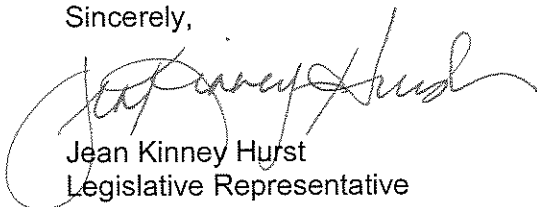
The several policy arguments are just as compelling. If the proponent's proposal were to become law, it would further invite a certain type of abuse whose use has accelerated rapidly over the past few years. Under these arrangements, a local jurisdiction agrees to refund to a retailer a certain percentage of the sales tax they generate – as high as 85% in some of the most recent cases – for artificially consolidating their state- or region-wide sales in one location within the city's limits. This belies the fact that the sales are in fact coming from many different jurisdictions. A small office of two or three individuals could funnel statewide sales to an out-of-state company in order to reap great financial rewards to the detriment of citizens in all of the jurisdictions where these products are actually being used. This is public money that is going directly to private hands with no resulting benefit to the general public. Sales and use taxes are critical to providing public services and facilities such as public safety and roadway maintenance to the residents of this state. Misusing them in this way not only diminishes these services and facilities, it increases the share of the tax burden borne by natural persons and less wealthy and influential companies, since the large companies that generate the most sales tax are the most lucrative and therefore most likely with which to make these sorts of arrangements.

The harm would be hugely exacerbated if the Board not only adopted this proposal, but also made it retroactive. Due to over two decades' worth of claims, the amount of money involved in a retroactive implementation of this proposal is staggering. It is important to keep in mind that this is not only public money against which many jurisdictions have bonded, but in the case of retroactive application this is money that jurisdictions have already spent on roads, peace officers, parks, water supply, health services and hospitals, et cetera. So the Board would be creating liabilities for nearly every local agency in the state, since according to the Board's analysis this change would negatively impact almost every jurisdiction, while having a positive effect on only a few. So the public-at-large would suffer due to an obscure regulatory change that is supported neither by statute nor by history.

Our final policy argument is that this change would irretrievably reallocate sales and use taxes across county lines. Under the California Constitution as amended by Proposition 1A (2004), "the Legislature shall not enact a statute to...change the method of distributing revenues derived under...the Bradley-Burns Uniform Local Sales and Use Tax Law." (Constitution of California Article XIII, Section 25.5(a)(2)(A).) While the Board's actions can usually be overturned by later actions of the state Legislature, in this case that is not a possibility. So any reallocations made by adopting this proposal could not be changed by anything short of a constitutional amendment.

In summary, the proposed change is not supported by, and is in fact directly in conflict with, statute; the proposed change is not supported by, and is in fact directly in conflict with, the historical record; the proposed change would redirect public money into private hands in two different ways, especially if implemented retroactively, increasing the tax burden on natural persons and less wealthy and influential companies and sending many jurisdictions into financial difficulty; and the proposed change would irretrievably reallocate revenues across county lines, short of a highly unlikely constitutional amendment. For all of these reasons, we ask that you reject this proposal.

Sincerely,



Jean Kinney Hurst  
Legislative Representative

cc: Jeffrey L. McGuire, Tax Policy Division (MIC 92)