Assembly Bill 2749 (Brough and Pan)
Date: 05/03/16
Program: Property Tax
Sponsor: United Rentals
Civil Code Section 1656.5 and Revenue and Taxation Code Part 13.7
Effective: January 1, 2017

Michele Pielsticker (Chief) 916.322.2376
Sheila T. Waters (Analyst) 916.445-6579
Ronil Dwarka (Revenue) 916.445.0840

Summary: Creates a rebuttable presumption that in a heavy equipment rental agreement the parties agreed to the addition of estimated personal property tax reimbursement ("reimbursement") to the heavy equipment rental price under specified conditions. Requires qualified heavy equipment renters to register with the BOE and remit any reimbursement collected in excess of the ad valorem property tax levied.

Summary of Amendments: Since the previous analysis, the bill was amended to require heavy equipment renters to register with the BOE and file an annual return, and require the BOE to collect any excess reimbursement pursuant to the Fee Collections Procedures Law (FCPL).

Purpose: According to the author, the purpose of this bill is to authorize rental companies to separately state an amount for property tax reimbursement and protect these companies from future legal challenges over this separately stated charge.

Fiscal Impact Summary: Indeterminable, but potential for a state General Fund revenue gain.

Existing Law: Under existing law,[1] all property is taxable unless specifically exempt under the Constitution or Revenue and Taxation Code. The county assessor determines taxability each year, generally on the January 1 lien date.

Personal property used in a trade or business is generally taxable. Property owners must file an annual business property statement with the county assessor to report the cost of the property.[2] The assessor values the personal property each lien date at its current fair market value. Generally, the assessor determines the current fair market value based on the property's acquisition cost with adjustments for inflation and depreciation.

The personal property tax rate is the same as the rate levied on real property. That rate is 1%, plus any local voter-approved indebtedness.

Regarding personal property taxation, California's Constitution[3] authorizes the Legislature by a 2/3 vote to classify personal property for different taxation or for exemption.

The law provides no specific tax exemption for heavy equipment leases or rentals (rentals). However, a personal property business inventory exemption[4] is available. Personal property intended for rent in the regular course of business that is *not* rented on the January 1 lien date is exempt from taxation for the upcoming fiscal year (July 1 to June 30). That property is regarded as business inventory on that particular day, even if the property is rented in the regular course of business for the other 364 days of the year.

Proposed Law: This bill creates a rebuttable presumption that, in a heavy equipment rental agreement, the parties agreed to the addition of estimated reimbursement to the heavy equipment rental price if all the following conditions occur:

(1) The rental agreement expressly provides for the addition of estimated reimbursement,

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[1] California Constitution Article XIII, Section 1, and Part 1 (commencing with Section 50) of Division 1 of the Revenue and Taxation Code (RTC).
[2] RTC Section 441.
[3] California Constitution Article XIII, Section 2.
[4] RTC Section 219.

(2) Estimated reimbursement is separately stated and charged on the rental agreement,

(3) The rental agreement states that the reimbursement amount charged is the renter's estimated personal property tax amount owed on that property for a specified lien date, and any excess amounts will be remitted to the Board of Equalization (BOE) for deposit in the state's General Fund.

(4) The reimbursement amount shall not exceed 0.75% of the heavy equipment's rental price.

The renter must remit the excess reimbursement with the return, and the BOE must deposit those amounts into the General Fund.

Administration. This bill requires the BOE to administer and collect any reimbursement pursuant to the Fee Collection Procedures Law (FCPL)[5] to the extent these provisions are not inconsistent with this act.

The FCPL generally provides for the BOE's administration of fee programs. Among other things, the FCPL provides for collection, reporting, return, refund, and appeals procedures, as well as the BOE's authority to adopt regulations related to the FCPL's administration and enforcement.

Registration, Reporting, and Payment. Every qualified renter must register with the BOE using a BOE-prescribed application, as described.

On or before September 30 each year (beginning in 2017), a qualified heavy equipment renter must file a return with the BOE for the preceding 12-month period ending August 31 on a form prescribed by the BOE. If the reimbursement collected exceeds the actual personal property tax levied for the previous fiscal year lien date, the excess amount constitutes a debt the qualified heavy equipment renter owes the state. The excess reimbursement collected is due and payable to the state annually on or before September 30 and must be paid in the form of remittances payable to the BOE. Both the application and the return may be authenticated in a form or pursuant to a method as the BOE may prescribe.

The bill specifies that any reimbursement collected shall conform to the Civil Code provisions added by this act.

Definitions. This bill defines the following terms:

- "Heavy equipment property" means a qualified heavy equipment renter's rental property.
- "Qualified heavy equipment renter" means a renter whose principal business is qualified heavy equipment rental and who is engaged in a line of business described in the North American Industry Classification System (NAICS) Codes 532412 or 532310, 2012 edition.
- "Rental price" means the total equipment rental charge, excluding any separately stated charges that are not rental charges, such as delivery and pickup fees, damage waivers, environmental mitigation fees, and sales tax reimbursement or use tax.

Legislative History: Three heavy equipment rental bills were considered during 2011-12 and 2013-14 Legislative Sessions. Unlike this bill, however, these measures imposed a tax on the heavy equipment rentals in lieu of the business personal property tax, as follows:

- AB 1941 (Ma, 2012) would have imposed a tax of 1.25% on a heavy equipment lease or rental.
- AB 1055 (Pan, 2013) would have imposed a tax at an unspecified rate on every qualified heavy equipment rentee.
- AB 2114 (Pan, 2014) would have imposed a 0.75% tax on a qualified heavy equipment renter.

The Assembly Revenue and Taxation Committee held AB 1941 and AB 1055, and Assembly Appropriations Committee held AB 2114.

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[5] RTC Part 30 (commencing with Section 55001).

Commentary:

1. **Effect of the bill.** Allows qualified equipment rental companies to seek reimbursement for personal property tax they owe on the equipment they hold for rent. Any excess reimbursement they collect must be remitted to the BOE for deposit into the state's General Fund.

2. **The May 3, 2016 amendments** create a new part within the Revenue and Taxation Code to provide for the administration and collection of the reimbursement pursuant to the FCPL. These amendments require heavy equipment renters to register with the BOE and file an annual return by September 30 for the preceding 12 month period ending August 31.

3. **Nothing prevents these rental companies from seeking reimbursement currently.** The law does not prohibit rental companies from separately stating a charge for reimbursement currently.

4. **To whom does this bill apply?** The bill states that a qualified heavy equipment renter is one whose *principal* business is in one of two NAICS Codes. NAICS code 532412 includes establishments primarily engaged in renting or leasing heavy equipment without operators that may be used for construction, mining, or forestry, such as bulldozers, earthmoving equipment, well drilling machinery and equipment, or cranes. According to the Employment Development Department's (EDD) labor market statistics, California has 557 firms under this classification.

   NAICS code 532310 includes establishments primarily engaged in renting a range of consumer, commercial, and industrial equipment. Establishments in this industry typically operate from conveniently located facilities where they maintain inventories of goods and equipment that they rent for short periods of time. The equipment types that establishments in this industry provide includes, but is not limited to, audio visual equipment, contractors' and builders' tools and equipment, home repair tools, lawn and garden equipment, moving equipment and supplies, and party and banquet equipment and supplies. EDD's statistics indicates California has 16 firms in this industry.

5. **Use tax will apply to the proposed property tax reimbursement amount.** Under the Sales and Use Tax Law,[6] any lease or rental of tangible personal property for a consideration is a "sale" and a "purchase" (except for certain items not relevant here). Generally, a lease of tangible personal property is regarded as a continuing "sale" and a continuing "purchase," and the use tax applies to the rental amount, including any payments required by the lease, such as amounts paid for personal property taxes on the leased property. The lessor is required to collect the use tax from the lessee at the time the rentals are paid by the lessee. Accordingly, any separately stated property tax reimbursement collected by a renter under this bill will be subject to the use tax.

Administrative Costs: BOE will incur administrative costs to implement and administer this bill, including programming costs to accommodate returns and payments, taxpayer notification costs, return and payment processing costs, and potentially audit workload costs. These costs are pending.

Revenue Impact:

Background, Methodology, and Assumptions. According to the U.S Census Bureau, 2012 Economic Census data, California receipts for these two industry groups are as follows:

NAICS Code 532412	$1.6 billion
NAICS Code 532310	215 million
Total	$1.8 billion

Based on IHS Global Insight's forecast, estimated rental receipts for 2017 will amount to $2.7 billion.

[6] Part 1 of Division 2 of the RTC, (commencing with Section 6001).

The bill specifies that the property tax reimbursement amount shall not exceed 0.75% of the heavy equipment's rental price. Applying the maximum 0.75% rate to the estimated \$2.7 billion in receipts results in \$21 million (0.75% × \$2.7 billion = \$21 million).

Sales and Use Tax. Staff assumes that the 0.75% property tax reimbursement is currently embedded in the equipment rental's price upon which use tax is imposed (assuming these rentals are continuing sales and continuing purchases where the lessor collects use tax on the rental receipts). Under this bill, the use tax would continue to apply to any separately stated property tax reimbursement amount authorized by this bill. Accordingly, staff does not anticipate any significant impact on sales or use tax revenues.

Property Tax. Staff does not have data regarding the property tax revenues heavy equipment renters pay currently. A 2013 Legislative Analyst's Office (LAO) report suggests that property tax on rental equipment would likely generate between \$20 million to \$25 million annually.

Revenue Summary. The bill requires any excess personal property tax reimbursement collected to be paid to the BOE for deposit into the state's General Fund. Based on the LAO estimated property tax on rental equipment range of \$20 million to \$25 million and the estimated property tax reimbursement amount of \$21 million, it is unclear whether the state's General Fund would realize a revenue gain.