



COUNTY OF RIVERSIDE AUDITOR-CONTROLLER'S OFFICE
Serving Riverside County since 1893

California Sales and Use Tax Training

June 3, 2010

Presented by:
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Introduction

- Jacob Bholat –Partner
 - Over 13 years in consulting with DSF and Deloitte
 - Primarily focused on Not for Profit and Government clients
 - Former State auditor with Board of Equalization
- Jim Fier – Managing Partner
 - Over 21 years in consulting with DSF and Deloitte
 - Former State auditor with Board of Equalization
- Steve Bixler – Senior Manager



Goals

- Provide an overview of the sales and use tax audit issues and findings
- Initiate discussion to help department leaders support their staff with sales and use tax compliance improvements

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Overview of Topics

- Overview of sales and use tax
- Areas of sales and use tax audit adjustments and steps for improvement
- Resource material (provided for reference only – will not be covered in presentation)

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Overview of Sales and Use Tax

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What is Sales & Use Tax?

- Excise tax
- Applies to tangible personal property (TPP)
- Transaction based
 - Sale – revenues generated by the County’s sales of TPP
 - Consumption – purchases of TPP used for County operations
- Presumption – all sales of TPP are subject to tax unless specifically exempted



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Responsibility for the Tax

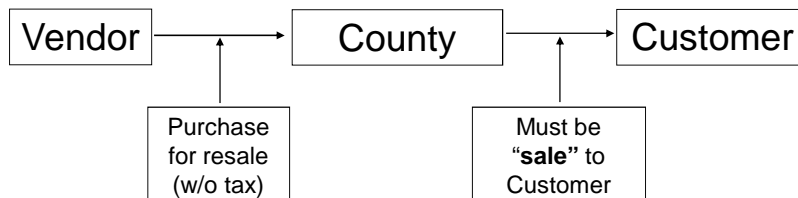
- ❑ County as buyer of TPP
 - **Applies to purchase and use of property in California**
 - Reimburse vendor for sales tax or use tax for out-of-state vendors
 - CA vendors (inform them if no tax billed)
 - There is no general exemption for County of Riverside
 - Accrue and pay use tax to state (A/P and purchasing)
 - Many non-California based sellers are not registered to collect tax. In such situations County pays directly to State
- ❑ County as seller of TPP
 - **Does not apply to charges for services provided by County**
 - Charge and collect sales tax on sales of TPP
 - Update Auditor Controller's Office when TPP sold
 - Use of Resale Certificate (limit certificate to items resold only)

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Purchases for Resale

- ❑ Activities with resale concerns:
 - Only use for activities where TPP purchased exclusively to resell
 - Limit resale certificate description to items resold only



Note: Resale certificate legally transfers liability for tax to buyer. Therefore, its issuance should be strictly controlled and issued through a central resource. One vendor could be selling product to multiple departments and not all may be reselling TPP

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Areas of Sales and Use Tax Audit Adjustments and Steps for Improvement

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Areas of Assessment

- ❑ Concessionaire operating on County property
 - Contract should clearly define responsibility for collecting and remitting sales tax to the State
 - Party/entity that operates/sells and collects revenue should be the party that reports tax
 - If vendor is responsible, confirm vendor is registered and complete proper certificate
 - Contract, certificates and tax information should be provided to Auditor Controller's office
 - Miscellaneous sales – Department should track miscellaneous revenue by department and provide support to Auditor Controller's Office
 - Responsible party identified to avoid duplicate reporting and to maintain proper documentation
 - Vending sales
 - Reports and other types of information provided in tangible form
 - Supplies sold to residents or other consumers
 - Sales of assets for disposal

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Areas of Assessment (continued)

- ❑ Use tax assessment
 - Ensure documentation availability (contracts, invoice etc)
 - Separate sales tax and freight when invoice is processed in system
 - Provide more detail of item description when requesting purchases and processing PO's
- ❑ Overpayments of tax
 - Software & maintenance
 - Delivered electronically exempt from tax – Key is to maintain proper documentation
 - Significant planning can be done prior to purchase of software
 - Invoice/Purchase Order/Contract should be consistent and provide information on delivery method of software/updates.
 - Construction contracts
 - Legal and other professional services
 - Exempt medicines for hospital

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Additional Steps

- Development of documentation retention protocols and procedures
 - Purchase invoice, contracts, sales invoices, resale certificates, etc.
- Materiality of Difference
 - Adjustment requests on any transactions should be weighed against cost of processing
 - Time spent on processing small adjustments takes away resources to review larger issues

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RESOURCE MATERIALS
Application of Tax
General Information
Provided for Reference Only

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Labor Charges

- Services unrelated to the sale of TPP are exempt
 - Consulting, legal, research, etc.

- Services related to the sale of TPP
 - **Exempt**
 - **Repair** – charges for restoring tangible personal property to its original condition
 - **Installation** – charges for labor or services used in installing or applying the property sold
 - Does not have to be separately stated
 - **Taxable**
 - **Fabrication** – labor which changes the identity of the tangible personal property from one form to another
 - **Assembly** – assembly charges for new products

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Computer Software

- ❑ Software (canned) - purchases of canned software including charges for license fees, site licensing, upgrades and other end user fees
 - TPP delivered – taxable
 - Delivered via Load-N-Leave – exempt
 - Delivered via telecommunication lines/downloads – exempt
- ❑ Software (custom)
 - More than 50% custom – exempt
 - Less than 50% custom – partially exempt

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Maintenance Contracts

- ❑ Hardware maintenance
 - Mandatory – taxable
 - Optional – exempt
- ❑ Software maintenance - Canned Software (off the shelf)
 - Mandatory – taxable
 - Optional
 - With tangible property - 50% exempt
 - Without tangible property - exempt
- ❑ Software maintenance – Custom Software (more than 50% of charges are for custom programming)
 - Mandatory – exempt
 - Optional - exempt

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Leases

- Leases (defined as “continuing sale or purchase”)
 - Rental, hire or license for tangible property
 - Temporary use of property
 - No bargain purchase option
 - Nominal buyout option – Lesser of one percent or \$100
 - (If nominal option, contract will be treated as an outright sale)
- Application of Tax
 - Default: Tax due on rental payments
 - Election: Lessor may elect to pay tax on its purchase price of the leased property in the first reporting period. Thereafter, no tax is due on rental payments.

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Leases (continued)

- Election Specifics
 - Irrevocable
 - Must occur in first reporting period after placing the property in rental inventory
- Compliance issues
 - State Board of Equalization audit policy looks to the Lessor for compliance
 - Lessee has limited visibility to payment of tax (per invoices)
 - Exclusions:
 - Use of property less for less than 24 hours & \$20 with restricted use; linens with laundry services; motion picture films or video tapes; household furnishing with living quarters; mobile transportation equipment (Lessor owes tax on its use); and
 - Tax-paid property in substantially the same form.

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Construction Contracts

- ❑ All contractors have a presence in CA and are obligated to properly administer the tax
 - **DSF's experience shows that most use tax accruals for construction contracts result in overpayments**
 - ❑ Contractor provides materials, fixtures and occasionally equipment under their contracts, generally:
 - Tax due on contractors cost of materials and fixtures, unless tax is billed
 - Contractors are retailers of equipment
 - ❑ Contractors may or may not charge tax on invoice
 - As consumers, contractors generally pay tax on their purchase of materials and fixtures installed and do not bill sales or use tax.
 - As retailers, contractors generally will collect tax on equipment sales
- KEY: Separately stated materials are not taxable sales

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Transportation

- ❑ Actual shipping charges by common carrier are exempt
- ❑ Shipping provided by retailers facilities are includable in the taxable selling price (if exempt sale, no tax on related shipping)
- ❑ Shipping and handling
 - Many vendors charge shipping and handling
 - Only the actual shipping costs by common carrier are excludable*
 - Handling charges are includable in the measure of tax

* Determining the actual shipping cost may be difficult and time consuming. An alternative is to use an estimated shipping and handling percentage to determine a taxable handling amount.

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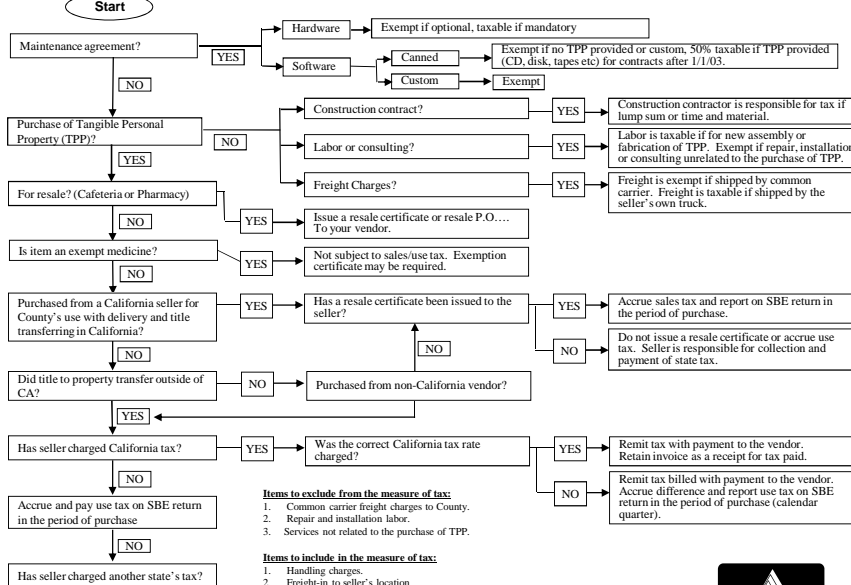


Other Exemptions

- ❑ Subscriptions – publications issued more than 4 times and less than 60 times a year are exempt
- ❑ Purchases from the U.S. Government and its instrumentalities are exempt
- ❑ Research and development contracts



Sales/Use Tax Quick Decision Chart for Purchases Appendix A



- Items to exclude from the measure of tax:**
1. Common carrier freight charges to County.
 2. Repair and installation labor.
 3. Services not related to the purchase of TPP.
- Items to include in the measure of tax:**
1. Handling charges.
 2. Freight-in to seller's location.

Notes:
 TPP: Tangible personal property;
 SBE: State Board of Equalization



Closing Statement

This seminar is intended to provide guidance for you. The seminar materials are limited to the California sales and use tax treatment of your sale and purchase transactions and may not apply to other industries or states.

The seminar materials are based upon the applicable law, regulations, and other tax authorities in effect as of the date of this presentation. We will update these materials upon your request.