



CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION

OFFICE OF THE DIRECTOR

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Director

May 3, 2024

Honorable Scott Wiener
Joint Legislative Budget Committee
1020 N Street, Room 553
Sacramento, CA 95814
Attention: Mr. Hans Herman

Dear Chairman Wiener:

Pursuant to Revenue and Taxation Code (RTC) section 6377.1 subdivision (g), this report summarizes the amount claimed by taxpayers subject to the partial sales and use tax exemption for manufacturing and research and development equipment in calendar year 2023. Additionally, this report summarizes the estimated amounts claimed due to the expansion of the exemption by Assembly Bill (AB) 398 (Ch. 135, Stats. 2017) for the purposes of transferring funds from the Greenhouse Gas Reduction Fund to the General Fund.

For calendar year 2023, actual amounts claimed on returns filed with the California Department of Tax and Fee Administration (CDTFA) resulted in lost sales and use tax revenue of \$464.8 million.

For the purposes of a transfer of funds from the Greenhouse Gas Reduction Fund and the General Fund, RTC section 6377.1 (g)(2)(B) requires the CDTFA to report on the total value of the exemption allowed for a qualified person that is either of the following:

- Primarily engaged in those lines of business described in Codes 221111 to 221118, inclusive, and 221122 of the North American Industry Classification System (Electric Utilities); or
- Primarily engaged in those lines of business described in Codes 3111 to 3399, inclusive, 541711 and 541712 of the North American Industry Classification System and is also a person that is an apportioning trade or business as described in paragraph (1) of subdivision (c) of RTC section 25128, that is required to apportion its business income pursuant to subdivision (b) of section 25128, or a trade or business as described in paragraph (1) of subdivision (c) of section 25128, conducted wholly within this state that would be required to apportion its business income pursuant to subdivision (b) of section 25128 if it was subject to apportionment pursuant to section 25101 (Agricultural Business Activities).

For calendar year 2023, \$130.7 million is the estimated amount claimed that is covered by these provisions. Please see the attached revenue estimate for the detailed methodology and calculation of this amount.

I hope the above information is helpful. If you have any questions regarding the revenue amounts claimed, please contact me at (916) 309-8300.

Sincerely,

Nicolas Maduros
Director

NM:ck

Attachment: Revenue Estimate, AB 398 Annual Report

cc: Senate.AgencyReports@sen.ca.gov

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CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION
REVENUE ESTIMATE

AB 398 Annual Report

REPORTING REQUIREMENT

Assembly Bill (AB) 398 (Chapter 135, Statutes of 2017) added a reporting requirement for the California Department of Tax and Fee Administration (CDTFA). Under Revenue and Taxation Code 6377.1(g) (2) (B) CDTFA is required to report on the total value of the manufacturing sales tax exemption attributed only to the expansion under AB 398 to electric utilities and agriculture business activities, as defined.

EXEMPTION SUMMARY BY CATEGORY AND METHODOLOGY

This reporting requirement results in partial exemptions claimed for three separate components: electrical utilities, agricultural businesses, and other manufacturers or research and development businesses (manufacturing). The basic source for breaking out the three components of total revenues is CDTFA's taxpayer reported tax return data. The registration data fields, among other things, contain the North American Industry Classification System (NAICS) codes and descriptions and the names of the entities claiming the exemptions. Based on our initial review, the breakdown of exemptions by category appears to be understated for electric utilities and agricultural business activities. The main reason for this seems to be that the reported NAICS codes are often associated with the retailer reporting the sale subject to the partial exemption rather than the consumer. To address this issue, we analyzed the return data in more detail, including manually reviewing many returns.¹

In calendar year 2023, CDTFA internal data show that manufacturing, electric utilities, and agriculture business activities exemptions totaled \$464.8 million. Based on our best assessment of the available data, below we have summarized the estimated breakout for each component.

	Calendar Year 2023 (\$ Millions)	Percent of Total
Electric Utilities	\$ 123,564,279	26.59%
Agricultural Business Activities	\$ 7,104,803	1.53%
Manufacturing	\$ 334,104,612	71.88%
Total Exemptions	\$ 464,773,694	100.00%

¹ As part of the manual review, for many companies, we researched company profiles and business activities on the internet.

QUALIFYING REMARKS

As noted above, often the exemption data is reported by the seller of the item and not the end user and many of the NAICS codes and descriptions in our data belong to the seller. This may impact the accuracy of the estimated breakdown for the three components, although we did our best to validate the data, including manually reviewing many entities claiming the exemptions. The accuracy of the total exemption amount is not impacted.

PREPARATION

Prepared by Tom Trach, Research and Statistics. For additional information, please contact Tom Trach at Tom.Trach@cdtfa.ca.gov or Genti Droboniku at Gentian.Droboniku@cdtfa.ca.gov.

Current as of March 21, 2024.