



STATE BOARD OF EQUALIZATION

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September 10, 2012

Honorable Katherine Feinstein, Presiding Judge
Superior Court of California
County of San Francisco
Civic Center Courthouse
400 McAllister St., Room 008
San Francisco, CA 94102

Dear Presiding Judge Feinstein:

In correspondence dated July 16, 2012, both the State Board of Equalization (BOE) and the Honorable Betty T. Yee, the BOE's Member from the First Equalization District, received notice that a response was required to a San Francisco Civil Grand Jury report: *Surcharges and Healthy San Francisco: Healthy for Whom?* This report, which documents the Jury's findings with respect to its investigation of several issues regarding the San Francisco Health Care Security Ordinance (SFHCSO), makes it clear that the BOE as an agency, and not Ms. Yee as an individual Board Member, is the responding party or entity that is required to respond to the relevant findings. Pursuant to California Penal Code section 933.5, a responding party or entity must either agree with the particular finding at issue or disagree with it in whole or in part, explaining the basis for any disagreement.

A review of the Jury's report indicates that Finding F3 states in part that the State of California, to the Jury's knowledge, has not "investigated whether sales tax is being added to the surcharges" and requests in part that the Board of Equalization (BOE) respond to the Jury's finding. Preliminarily, we believe it would be helpful to explain the imposition and application of tax in general. The California Sales and Use Tax Law imposes a sales tax upon retailers for the privilege of selling tangible personal property at retail in the State of California. The use tax is complementary to the sales tax and is imposed, when sales tax does not apply, upon the consumer for the storage, use or other consumption of tangible personal property in the State of California. Either the sales tax or the use tax applies to all retail sales of tangible personal property to consumers in California, unless otherwise exempted by statute or type of transaction. When subject to tax, the kind of transactions discussed in the report will generally be subject to sales tax, not use tax. The measure of tax (i.e., the amount of the "total selling price" to which the applicable tax rate is applied) for a transaction subject to sales tax is called "gross receipts."

California Revenue and Taxation Code section 6012, provides that "gross receipts" mean in part the total amount of the sale or lease or rental price, as the case may be, of the retail sales of retailers, valued in money, whether received in money or otherwise, except for the cost of the property sold; the cost of the materials used, labor or service cost, interest paid, losses, or any

other expense; and the cost of transportation of the property (except as excluded by other provisions of this section). As such, surcharges added to the sale of tangible personal property generally are included in gross receipts.

We respectfully disagree with the finding that the BOE has not investigated whether retailers have added sales tax to SFHCO surcharges. The BOE has active audit and compliance programs to ensure the correct application and remittance of sales and use tax by all taxpayers. This agency does its best to verify that all taxpayers have accurately collected and remitted sales and use taxes in accordance with Sales and Use Tax Law. For example, as a result of investigations conducted in 2009, it was determined that certain retailers, primarily restaurant establishments, did not calculate and remit sales tax on SFHCSO surcharges added to their sales of tangible personal property. To inform taxpayers of their responsibility regarding the application of tax to SFHCO, we prepared the enclosed copy of the April 2009 Special Notice, *Sales Tax Applies to the San Francisco Health Care Security Ordinance Surcharge*, and mailed copies (approximately 26,000) to all businesses with a registered location in San Francisco. A copy of the special notice also is posted on the BOE's website for all affected retailers and other interested parties to view at <http://www.boe.ca.gov/news/pdf/1224.pdf>.

The special notice provides guidance to retailers regarding the application of tax to the SFHCSO surcharge. The special notice explains in part:

Under this ordinance, qualifying businesses located within San Francisco are required to provide a mandated minimum health care benefit to their employees. To defray the cost, many businesses have raised their prices on the goods and services they sell. However, some businesses have chosen to add a surcharge to their receipts instead of raising their selling prices. The surcharge may either be a flat fee or a percentage of the selling price. 'Please note, when a surcharge is separately added to any taxable sale, the surcharge is also subject to sale tax.'

The notice provides two examples of the computation of sales tax to a taxable sale with SFHCSO surcharges added, one as a flat fee and one as a percentage of the sale. In both examples, tax is applied to the total selling price, including, the SFHCO surcharge, and is examined as a part of routine audits. These routine audits constitute regular and ongoing investigative activity by the BOE with respect to proper application of the Sales and Use Tax Law to the SFHCO surcharge. The BOE is precluded from publicizing the specific results of these audits due to legal restrictions on the disclosure of confidential taxpayer information (e.g., Revenue and Taxation Code section 7056.)

Without violating the confidentiality rights of specific taxpayers, we can comment that a review of audits conducted by our San Francisco District office since implementation of the SFHCSO to the present establishes that auditors identified taxpayers that did not include separately stated amounts for the SFHCO surcharge in reported taxable gross receipts. In cases in which the taxpayer did not include separately stated amounts for the surcharge in taxable gross receipts, the auditor assessed additional tax on the unreported surcharge.

As stated above, the BOE is committed to verifying that all taxpayers have accurately collected and remitted sales and use taxes in accordance with Sales and Use Tax Law. BOE will continue to investigate employers' practices regarding sales tax reimbursement collection on the measure of the surcharge, when separately stated, pursuant to our ongoing audit and compliance programs.

I hope this information is helpful. If there are any questions regarding this response, please call me at (916) 324-2916 or you may contact me via e-mail at trista.gonzalez@boe.ca.gov.

Sincerely,

Trista Gonzalez, Supervisor
Audit and Information Section

THG:lsc:dmt

Enclosure: Special Notice, *Sales Tax Applies to the San Francisco Health Care Security Ordinance Surcharge*, April 2009

cc: Honorable Betty T. Yee, Member, First District
Mr. Alan LoFaso (MIC 71)
Ms. Cynthia Bridges (MIC 73)
Mr. Jeffrey L. McGuire (MIC 43)
Mr. Randy Ferris (MIC 83)
Ms. Susanne Buehler (MIC 92)

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bc: Mr. Jason Parker (via e-mail)
Mr. Brad Miller (MIC 92)
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Mr. David Theiss (via e-mail)
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