

AN ALERT FROM THE BDO STATE AND LOCAL TAX PRACTICE

# BDO KNOWS:

## SALT



### ► SUBJECT

## MANUFACTURING EXEMPTION GOES INTO EFFECT FOR REDUCED SALES AND USE TAX IN CALIFORNIA BEGINNING JULY 1, 2014.

### ► SUMMARY

Legislation enacted in California in 2013 provides that, beginning July 1, 2014, and extending until June 30, 2022, a “qualified” purchaser or lessee of R&D or manufacturing equipment will be eligible to obtain a partial exemption of the sales and use tax. While the exemption does not apply to the city, county, or district sales taxes, a qualified purchase from July 1, 2014, through December 31, 2016, would receive a reduction in the state sales and use tax rate from 7.5% to 3.3125%. After 2016, the exemption amount is slated to be slightly reduced, resulting in a slight increase in the applicable states sales and use tax rate.

### ► DETAILS

In order to qualify for the exemption, you must be a “qualified” person purchasing “qualified” property which will have a “qualified” use. The exemption is available for qualified businesses classified under specified 2012 North American Industry Classification System codes 3111-3399 (manufacturing), 541711 (biotech research and development), and 541712 (physical, engineering, and life sciences research and development). Businesses in other industries are ineligible for the exemption.

Qualified tax-exempt property could include machinery and equipment; equipment and devices used or required to operate, control, regulate, or maintain the machinery; pollution control items; and certain special purpose buildings and foundations. Qualifying purchases cannot exceed \$200 million in any calendar year per qualified person or combined reporting unit. Please note that the periods of July 1, 2014, through December 31, 2014, and January 1, 2022, through June 30, 2022, are not prorated with respect to the annual limitation.

### CONTACT:

#### WEST:

**ROCKY CUMMINGS**, Tax Partner  
415-490-3130 / rcummings@bdo.com

**PAUL MCGOVERN**, Tax Senior Director  
714-913-2592 / pmcgovern@bdo.com

#### NORTHEAST:

**JANET BERNIER**, Tax Principal  
212-515-5405 / jbernier@bdo.com

**MATTHEW DYMENT**, Tax Senior Director  
617-239-4130 / mdyment@bdo.com

**MARK SEIDEN**, Senior Director  
212-885-8004 / mseiden@bdo.com

#### SOUTHEAST:

**ASHLEY MORRIS**, Tax Senior Director  
919-278-1963 / amorris@bdo.com

#### ATLANTIC:

**JONATHAN LISS**, Tax Senior Director  
215-636-5502 / jliss@bdo.com

**JEREMY MIGLIARA**, Tax Senior Director  
703-770-0596 / jmigliara@bdo.com

#### CENTRAL:

**ANGELA ACOSTA**, Tax Senior Director  
248-688-3313 / aacosta@bdo.com

**NICK BOEGEL**, Tax Senior Director  
414-615-6773 / nboegel@bdo.com

**JOE CARR**, Tax Principal  
312-616-3946 / jcarr@bdo.com

**GENE HEATLY**, Tax Senior Director  
214-665-0716 / gheatly@bdo.com

**MARIANO SORI**, Tax Partner  
312-616-4654 / msori@bdo.com

**RICHARD SPENGLER**, Tax Senior Director  
616-776-3687 / rspengler@bdo.com

To qualify for the exemption, the property must be used at least 50 percent in one of the following activities:

- Manufacturing, processing, refining, fabricating, or recycling tangible personal property;
- Researching and developing; or
- Maintaining, repairing, measuring, or testing any qualified property.

Items that do not qualify for the exemption include consumables with a useful life of less than one year, furniture and equipment used to store completed products once the manufacturing process is completed, and property used primarily in administration, general management, or marketing.

Additionally, the exemption is deemed inapplicable if, within one year from the date of purchase, the purchaser either:

- uses the property in a manner that does not qualify for the exemption;
- converts the property from an exempt use to a nonqualifying use; or
- removes the qualifying property from California.

The California State Board of Equalization (“BOE”) has provided an overview of the exemption, qualifications required for the exemption, and documentation steps to take for both the sellers and purchasers of the “qualified” equipment.<sup>1</sup>

The BOE should make available on its Web site in July, 2014, certificates to use for documenting the partial exemption. In the interim, the Web site contains examples of certificates.<sup>2</sup>

## ► BDO INSIGHTS

Qualified manufacturers and companies performing research and development in the fields of physical, engineering, and life sciences or biotechnology should consider taking the necessary action steps after July 1, 2014, to take advantage of this partial sales and use tax exemption. Estimated savings of \$4,100 on a qualified purchase of \$100,000 should not be ignored. Unless the customer provides an exemption certificate to obtain the reduced rate, sellers of qualifying property should continue to collect the full 7.5% state sales tax rate. The BOE has also provided additional information on the reduced rate in a discussion paper distributed in early 2014.<sup>3</sup> BDO’s national sales and use tax team can help provide your company guidance in understanding the qualifications and implementation of this new California exemption.

<sup>1</sup> The document may be viewed at [www.boe.ca.gov/sutax/manufacturing\\_exemptions.htm#Overview](http://www.boe.ca.gov/sutax/manufacturing_exemptions.htm#Overview).

<sup>2</sup> The examples may be viewed at [www.boe.ca.gov/pdf/boe230m.pdf](http://www.boe.ca.gov/pdf/boe230m.pdf) (for the lease of manufacturing, research, and development equipment) and [www.boe.ca.gov/pdf/boe230mc.pdf](http://www.boe.ca.gov/pdf/boe230mc.pdf) (construction contracts for manufacturing, research, and development equipment).

<sup>3</sup> The discussion paper may be viewed at [www.boe.ca.gov/meetings/pdf/1525-4TDPweb.pdf](http://www.boe.ca.gov/meetings/pdf/1525-4TDPweb.pdf).

The Tax Practice at BDO is among the largest tax advisory practices in the United States. With 49 offices and more than 400 independent alliance firm locations in the United States, BDO has the bench strength and coverage to serve you.

BDO is the brand name for BDO USA, LLP, a U.S. professional services firm providing assurance, tax, financial advisory and consulting services to a wide range of publicly traded and privately held companies. For more than 100 years, BDO has provided quality service through the active involvement of experienced and committed professionals. The firm serves clients through 49 offices and over 400 independent alliance firm locations nationwide. As an independent Member Firm of BDO International Limited, BDO serves multinational clients through a global network of 1,264 offices in 144 countries.

BDO USA, LLP, a Delaware limited liability partnership, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms. BDO is the brand name for the BDO network and for each of the BDO Member Firms. For more information, please visit [www.bdo.com](http://www.bdo.com).

*To ensure compliance with Treasury Department regulations, we wish to inform you that any tax advice that may be contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax-related penalties under the Internal Revenue Code or applicable state or local tax law provisions or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein.*

*Material discussed in this tax alert is meant to provide general information and should not be acted on without professional advice tailored to your firm's individual needs.*