

**Text of Proposed Changes to**

**Title 18. Public Revenues**

**Regulation 1602.5. Reporting Methods for Grocers.**

(a) Food Products Exemption - In General (unchanged).

(b) Reporting Methods.

(1) Purchase-Ratio Method. ....(unchanged):

(A) (unchanged).

(B) (unchanged).

(C) (unchanged).

(D) (unchanged).

(E) The records should be complete and adequate, and all sales and purchases should be properly accounted for in the records. All purchases of exempt food products, grocery taxable items and nongrocery taxable items should be segregated into their respective classifications.

(F) The following definitions apply to the purchase-ratio method:

1. "Exempt food products" means those items generally described as food products in Section 6359 and Regulation 1602. If grocers are uncertain as to the classification of any product, they should contact the nearest ~~department~~board office.
2. "Total gross receipts from the sale of grocery items" means the total amount of the sales price of all exempt food products and taxable grocery items, including sales tax reimbursement, amounts receivable from manufacturers, or others, for coupons (excluding any handling allowances) redeemed by customers, and the face value of CalFresh benefits~~federal food stamps~~. The term does not include receipts from sales of those items described in (b)(1)(B), above, which are commonly referred to as "nongrocery taxable items," or from those sales described in (b)(1)(C), above (gasoline, snack bar, etc.). It does not include amounts which represent "deposits," as defined in Regulation 1589, e.g., bottle deposits. When deposits are not segregated, it will be presumed, and in the absence of evidence to the contrary, that the total deposits received are equal to the deposits refunded.
3. (unchanged).
4. (unchanged).

a~~A~~. As used herein, the term "cash discount" means a reduction from the invoice price which is allowed the grocer for prompt payment.

bB. As used herein, the term “volume rebate or quantity discount” means an allowance or reduction of the price for volume purchases based on the number of units purchased or sold. Such rebates or discounts normally are obtained without any specific contractual obligation upon the part of the grocer to advertise or otherwise promote sales of the products purchased. The term does not include patronage dividends distributed to members by nonprofit cooperatives pursuant to Section 12805 of the Corporations Code, or rebates which constitute a distribution of profits to members or stockholders.

cC. As used herein, the term “promotional allowance” means an allowance in the nature of a reduction of the price to the grocer, based on the number of units sold or purchased during a promotional period. The allowance is directly related to units sold or purchased although some additional promotional expense may be incurred by the grocer. Normally, grocers would feature the product in their advertising, although they may or may not be contractually obligated to do so.

The retail price of the product may or may not be lowered during a promotional period.

The term does not include display or other merchandising plan allowances or payments which are based on agreements to provide shelf space for a price not related to volume of purchases, or cooperative advertising allowances which are based on a national line rate for advertising and are not directly related to volume of purchases and sales. Cooperative advertising allowances are intended to reimburse grocers for a portion of their advertising costs for a particular product or products.

(G) Sales tax reimbursement collected in accordance with Regulation 1700 which is included in total sales is an allowable deduction. An example of the computation of the purchase-ratio method which provides for an adjustment for sales tax included follows:

1. Taxable grocery purchases .....	\$40,000
2. Add sales tax adjustment (8.25% * x Item 1) .....	3,300
3. Adjusted taxable grocery purchases (Item 1 + Item 2) .....	43,300
4. Exempt food products purchases .....	130,000
5. Total grocery purchases including sales tax (Item 3 + Item 4)...	173,300
6. Exempt food products ratio (Item 4 divided by Item 5).....	75.01%
7. Total sales including sales tax .....	254,088
8. Nongrocery taxable sales including sales tax if such sales are not accurately segregated, mark up nongrocery taxable cost of goods sold to compute sales-add 8.25% * sales tax to total) ** .....	31,500
9. Grocery sales including sales tax (Item 7 - Item 8) .....	222,588
10. Exempt food products sales (Item 6 x Item 9).....	166,963
11. Sales of taxable items including sales tax (Item 7 - Item 10) .....	87,125

12. Less taxable items purchased with <u>CalFresh benefits food stamps</u> (2% of total <u>CalFresh benefits food stamps</u> redeemed for period, e.g., 2% x \$100,000) .....	2,000
13. Taxable Measure including sales tax (Item 11 - Item 12) .....	85,125
14. Sales tax included (8.25/108.25* x Item 13) .....	6,488
15. Measure of tax (Item 13 - Item 14) .....	78,637
16. Sales tax payable (8.25%* x Item 15) .....	6,488

(2) Modified Purchase-Ratio Method ..... (unchanged).

(3) Retail Inventory Method and Markup Method. .... (unchanged):

(A) Retail Inventory Method.

1. (unchanged).
2. (unchanged).
3. (unchanged).
4. (unchanged).
5. (unchanged).
6. (unchanged).

(B) Cost Plus Markup Method - Taxable Merchandise.

1. (unchanged).
2. (unchanged):

aA. Markup factor percentages<sup>1</sup> applicable to taxable merchandise should be determined by a shelf test sample of representative purchases, covering a minimum purchasing cycle of one month within a three-year period, segregated by commodity groupings, i.e., beer, wine, carbonated beverages, tobacco and related products, paper products, pet food, soap, detergents, etc. The markup factor percentages determined for commodity groupings should be applied to the cost of sales of the respective commodities for the reporting period to determine taxable sales.

In order to ~~ensure~~insure that markup factor percentages typical of the total business are determined, grocers who conduct multistore operations should include purchases from several representative stores in the shelf test sample of markup factor percentages.

bB. As an alternative procedure to A., above, the overall average markup factor percentage for all taxable commodity groupings may be used to determine taxable sales for the reporting period. This markup factor percentage is applied to the overall cost of taxable sales for the reporting period.

The overall average markup factor percentage should be determined as follows:

ia. Determine markup factor percentages by commodity groupings based on shelf tests covering a minimum purchasing cycle of one month within a three-year period.

ii. Determine cost of sales, segregated by commodity groupings, for a representative one-year period.

iii. Apply markup factor percentages (Step a) to the cost of sales of the respective commodity groupings (Step b) to determine anticipated sales by commodity groupings and in total.

iv. Divide total anticipated sales (Step c) by the respective total cost of sales to determine the overall average markup factor percentage.

cE. In calculating markup factor percentages, appropriate consideration should be given to markon and markdown price adjustments, quantity price adjustments such as on cigarettes sold by the carton, liquor sold by the case and other selling price adjustments. Quantity and other price adjustments may be determined by a limited test of sales of a representative period or by sales experience of a representative store within the operating entity.

dD. The computation of taxable sales for the reporting period should be based on cost of sales for the period. If for any particular reporting period or periods, cost of sales is not determinable because actual physical inventories are unknown and inventories remain substantially constant, the computation of taxable sales may be based on purchases for the period. However, if inventories are not substantially constant, adjustments for physical inventories should be taken into consideration in one of the reporting periods occurring within the accounting year.

eE. Shrinkage should be adjusted as specified in (d) below.

fF. Taxable markup factor percentages based on shelf test samples will generally be considered valid for reporting purposes for a period of three years, provided business operations remain substantially the same. A substantial change in business operations will be considered as having occurred when there is a significant change in pricing practices, commodities handled, commodity mix, locations operated, sources of supply, or other circumstances affecting the nature of the business.

(4) Electronic Scanning Systems ..... (unchanged).

(c) CalFresh Benefits (Formerly Food Stamps). Tangible personal property eligible to be purchased with CalFresh benefits~~federal food stamps~~ and so purchased is exempt from the tax. Grocers who receive gross receipts in the form of CalFresh benefits~~federal food stamp coupons~~ in payment for such tangible personal property which normally is subject to the tax, e.g., nonalcoholic carbonated beverages, may deduct on each sales tax return an amount equal to two percent (2%) of the total amount of CalFresh benefits~~food stamps~~ redeemed during the period for which the return is filed. ~~Effective January 1, 1993, grocers~~Grocers may claim amounts in excess of two percent whenever the following computation results in a greater percentage: total purchases of taxable items eligible to be purchased with CalFresh benefits~~federal food stamps~~ divided by an amount equal to the total of the exempt food product purchases as defined in subdivision (b)(1)(F)<sup>1</sup> plus the purchases of taxable items eligible to be purchased with CalFresh benefits~~federal food stamps~~. For example, for a reporting period, if the total purchases of carbonated beverages equals \$5,000 and the total purchases of exempt food products equals \$130,000, a percentage of 3.7% ( $\$5,000 \div \$135,000$ ) may be used in computing the allowable CalFresh benefits~~food stamp~~ deduction for that period. This deduction may be taken in lieu of accounting separately for such sales.

(d) Shrinkage ..... (unchanged):

(1) (unchanged).

(2) (unchanged).

(e) List of Methods Not Exhaustive ..... (unchanged).

(f) Audits. Taxpayers using one of the approved methods of reporting described in this regulation will normally be audited by application of the same approved procedure in the audit to verify the accuracy of claimed deductions. However, determinations may be imposed or refunds granted if the ~~department~~board, upon audit of the retailer's accounts and records, determines that the returns did not accurately disclose the amount of tax due.

\* . . . (unchanged).

\*\* . . . (unchanged).

<sup>1</sup> . . . (unchanged).

Note: Authority cited: Sections 7051 and 7051.5, Revenue and Taxation Code-, Sections 15570.22 and 15570.24, Government Code. Reference: Sections 6359 and 6373, Revenue and Taxation Code.

---