



ISSUE UPDATE

DIRECT PAYMENT PERMITS



REGULATION 1699.6 Self Assessment of Use Tax Obligations

The California Department of Tax and Fee Administration (CDTFA) permits California business to self-assess their use tax obligations. This does not increase use tax due but does allow businesses to apply for and obtain a direct payment permit from the CDTFA. To qualify for a permit, a business must have had purchases and/or leases of at least \$500,000 subject to use tax in the prior calendar year and have a seller's permit or consumer use tax permit.

Once obtained, a direct payment permit allows the holder to avoid paying use tax to its out-of-state vendors. Instead, the business issues to vendors a use tax exemption certificate. The certificate declares that the buyer or lease will pay the tax directly to the CDTFA on its quarterly tax return.

BENEFITS OF SELF-ASSESSMENT

The self-assessment rules were sponsored by the California Manufacturers Association to achieve three key benefits:

- 1. To provide companies with better control over its use tax liability.** Under California law, the liability for the use tax is with any person consuming property in the state. Some out of state vendors may collect the tax, but that does not necessarily relieve the consumer of their liability. By issuing exemption certificates to all out-of-state vendors, use tax responsibility is in the hands of the consumer. This allows the consumer to determine when tax applies to their purchases instead of relying on the decisions of an out of state seller. It also simplifies the method used to self-assess the use tax as no tax is paid directly to out-of-state vendors.
- 2. To provide improved management of cash flow.** With self-assessment, a business pays its use tax quarterly rather than each time a taxable purchase is made. The delay between the time the tax is accrued and the time it is paid allows cash to be put to better uses. Furthermore, in those instances where the property is received and temporarily stored in California then subsequently shipped out-of-state for use, there would be no need to seek a refund.
- 3. To improve the quality of local support services.** Use taxes paid by self-assessment accrue to the local jurisdiction where the item or material acquired is first placed into functional use. This means that the city or county where your business is located can receive a direct benefit from your use taxes. Without self-assessment, the use tax is "pooled" and then shared between jurisdictions in the county on formula basis. Self-assessment allows more of your tax dollars to support your local police, fire, and other services that benefit your company and employees.

REQUIREMENTS FOR A PERMIT

A direct payment permit will be issued only if all the following conditions are met:

1. The applicant holds a valid seller's permit.
2. The applicant agrees to report and pay directly to the CDTFA all tax liabilities which are transferred from retailers to the applicant as a result of exemption certificates issued in accordance with this regulation.
3. The CDTFA determines that issuance of the direct payment permit will facilitate the collection of the tax. This requirement will be met only if the applicant has sufficient information processing resources to accurately and timely account for and report the tax liabilities assumed as a result of the direct payment permit (separately from other tax liabilities) and allocate the local tax portion of such liabilities to all of the cities, counties, redevelopment agencies, and districts involved.

4. The CDTFA determines that issuance of the direct payment permit is to the mutual convenience of the board, the applicant, and the retailers whose tax liability will be reported and paid by the applicant. Issuance of the permit will not be deemed to be to the convenience of the CDTFA if the applicant is a government entity or if the applicant has had gross receipts from sales of tangible personal property of less than \$75,000,000 and purchases of tangible personal property subject to sales or use tax of less than \$75,000,000 in any calendar quarter during the twelve months immediately preceding the application for the permit.
5. The applicant has a record of timely payment of tax liabilities and is in such financial condition that issuance of the direct payment permit will not result in a tax loss to the state.

HOW TO APPLY

The process for obtaining a Use Tax Direct Payment is simple. You may discontinue the permit at any time by notifying the CDTFA.

1. **Complete Form CDTFA-400-DP.** The application should be completed and signed by an officer of the organization, preferably the individual responsible for preparing the California Sales and Use Tax Return. The form can be found on the CDTFA's website by going to <https://www.cdtfa.ca.gov/formspubs/cdtfa400dp.pdf>. Be sure to answer each question and be prepared to include the items listed below.
2. **Statement of Cash Flows.** A simple spread sheet that shows 10 to 15 purchases subject to use tax (that took place in the prior calendar year) is adequate. The total of the purchases would need to exceed \$500,000. A purchase subject to use tax is an item that shipped from outside of California. A purchase of imaging equipment, hospital beds, medical supplies, warehouse equipment, manufacturing machinery, or any item that shipped to you from a point out-of-state would be a purchase subject to use tax. The CDTFA would prefer the format below:

Date	Invoice #	Item Description	Vendor	Cost
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**Note: Any local agency can apply for and receive a Direct Payment Permit without providing a Statement of Cash Flows.*

3. **Written Statement.** In addition to the application and spreadsheet, the CDTFA requires a written statement (on your corporate or letterhead) indicating that the organization had purchases subject to use tax in the prior calendar year that were in excess of \$500,000. The letter and the application should be signed by the same individual.

If you choose to go forward with the application, the CDTFA's processing time is about two weeks. After the application is approved, you will receive a new resale certificate and an exemption certificate. Your CDTFA account number will remain the same. You will send copies of the exemption certificate to your out of state vendors and keep the original for your records.

WHAT HAPPENS NEXT?

Self-assess and pay your tax liability using your existing CDTFA account. When your business or agency buys equipment or material subject to use tax, do not pay the tax to the out-of-state vendor. Instead, give the vendor a completed Exemption Certificate. When your quarterly Sales and Use Tax Return is filed, include the total use tax amount on the "Purchases Subject to Use Tax" line.

FREQUENTLY ASKED QUESTIONS

- **Is self-assessment required?**
No. Acquiring and using a direct payment permit is strictly voluntary and was devised to allow companies to take advantage of the benefits of self-assessment.
- **Will my company's tax liability increase?**
No. Self-assessment changes the way use tax is collected but does not change the amount owed.
- **Will this increase accounting costs?**
No. Self-assessment simplifies the use tax accrual process for taxpayers because a single class of "non-taxed" purchases is created for purchases from out of state vendors.
- **If I self-assess, what happens to the use tax the vendor collects?**
For transactions where you elect to self-assess, you pay no use tax to the out of state vendor. Instead, you issue an exemption certificate to the vendor. Once a certificate is issued for a transaction, an out-of-state vendor has no further obligation to the state to collect state use tax from that sale.
- **Won't this mean a lot of red tape?**
No. The process is easy and accounting effort could be reduced.
- **If I elect to self-assess, must I always self-assess?**
No. You may decide to discontinue self-assessment at any time. After a period of inactivity, CDTFB may revoke your direct payment permit, but there is no penalty for this.