



MTC State Tax Compliance Initiative

2004 FTA Annual Meeting
Tuesday, June 8, 2004
R. Bruce Johnson
Commissioner, Utah State Tax Commission
Chair, Multistate Tax Commission



State Tax Compliance Initiative—Purposes

- Identify Major State Tax Compliance Problems
- Develop Solutions for Improving Compliance
- Implement Solutions on State-by-State and Cooperative Basis

Why Tax Compliance Is Important

- Equity—Diligent Taxpayers Should Not Bear a Greater Tax Burden Due to Underpayments by Other Taxpayers
- Integrity—Non-compliance Encourages More Non-Compliance and Disrespect for Tax Systems
- Effectiveness—Taxes Levied by Legislative Authorities to Should Be Properly Collected.

Estimating the Compliance Gap

- \$6-\$9 billion in underreported sales and use tax—by registered and non-registered sellers (Projected from MN study)
- \$8-\$9 billion in uncollected tax on remote sales—by sellers with or without nexus (Projected from MN study)
- \$10-\$17 billion in Corporate Income Tax Sheltering (domestic & international) (MTC \$9-\$13 billion + \$2-\$4 billion from other studies)
- \$1.5-\$12 billion in underreporting of Pass-Through Entity Income (Projected from IRS Reports)

Total Estimated Annual Tax Gap – \$25-\$47 billion

Sources of Compliance Problems

- Growing Complexity of Economy and Business Operations
- Outdated or Insufficient Tax Policies and Practices
- Limited Enforcement Resources
- Increasingly Aggressive Tax Planning

State Tax Compliance Initiative—Organizational Structure

- Steering Committee
 - ◆ Elizabeth Harchenko (OR), Chair
 - ◆ Chairs of the three work groups
- Three Work Groups:
 - ◆ Sales and Use Tax {14 states}—Carol Fischer (MO)
 - ◆ Corporate Income Tax Sheltering {13 states}—Gerald Goldberg (CA-FTB)
 - ◆ Pass-through Entity Shareholder Reporting {9 states}—Elizabeth Harchenko (replacing former chair, Phil Brand (DC))

Sales and Use Tax Compliance Issues

- Use tax remittance by business consumers
- Use tax remittance by household consumers
- Use tax collection by remote sellers with nexus, and encouragement of voluntary collection by remote sellers without nexus.

Sales and Use Tax Compliance—Recommendations Approved

- More Effective Education of Taxpayers and Tax Practitioners
- Promote Awareness of Existing MTC Voluntary Disclosure Program
- Proposed Uniform Affiliate Nexus Statute or Regulation
- Enhance Exchange of Information Among States

Corporate Income Tax Sheltering Problems

- Entity Isolation (e.g., Intangibles Holding Companies, Securities Holding Companies, Corporate Inversions)
- Lack of Uniformity (e.g., Inconsistent Reporting, Structural Non-uniformity among States)
- Assignment of Sales of Other than Tangible Personal Property
- Federal Impact on State Taxation

Corporate Income Tax Sheltering—Proposals under Consideration

- Combined Reporting
- Enact Expense Disallowance Statutes (intermediate step towards combined reporting)
- Overhaul UDITPA—especially needed for sales of services & intangibles; financials industry
- Adopt Throwback Rules—to limit “nowhere income”

Corporate Income Tax Sheltering—Proposals under Consideration

- Require Disclosure of Filing Positions
- Tax Shelter Information Sharing and Listed Transactions Legislation
- Proactive Role in Federal Legislation
- Enhance Exchange of Information

Pass-through Entity Compliance Issues

- Rapid growth in number and income share of pass-through entities
 - ◆ S-Corporation and partnership growth:
 - 1.4 million in 1985
 - 3.1 million in 1990
 - 5.1 million in 2001
 - ◆ Share of reported business net income grew from **9.2% in 1990** to **42.3% in 2001**.

Pass-through Entity Compliance Issues

- Difficulty in tracking pass-through entity income
- Owners' difficulties in determining how to report and pay tax owed
- Difficulty in understanding how owners are using these entities.

Pass-through Entity Compliance—Ideas under Discussion

- Develop administrative systems that ease filing requirements for owners of pass-through entities, especially nonresident owners (e.g., MTC's Uniformity Proposal for Reporting Options for Nonresident Members of Pass-through Entities)
- Develop administrative systems to verify owners of pass-through entities pay taxes to states from which income is earned

Pass-through Entity Compliance—Ideas under Discussion

- Develop Educational Resources on Pass-through Entities for the States
- Expand Federal-State Compliance Efforts with respect to Proper Reporting of Pass-through Entity Income

MTC State Tax Compliance Initiative

- States Invited to Join Compliance Initiative
- Business Community Invited to Suggest Additional Compliance Improvements