

Joint Cost of Collection Study: What Is It? What Does It Say?

Presentation of Elliott Dubin, Director of Policy Research
Multistate Tax Commission
Federation of Tax Administrators Annual Meeting
Little Rock, Arkansas
June 7, 2006

Joint Cost of Collection Study: What Is It?

- A joint public/private sector group, working through the Streamlined Sales Tax Project (SSTP), organized to determine what costs retailers incur for the collection of sales and use taxes-- including costs shifted from vendors to state governments—of changes to the system proposed by the Streamlined Sales Tax Project .
- Sponsoring organizations: National Retail Federation; Council on State Taxation; Multistate Tax Commission; Federation of Tax Administrators; National Conference of State Legislatures

Joint Cost of Collection Study: What Is It?

- Prime Contractor is PriceWaterHouseCoopers
- Subcontractors are: National Opinion Research Council and Erard Associates
- Academic Advisory Council (James Alm Georgia State U., Therese McGuire Northwestern U., and Gary Cornia Brigham Young U.) oversee that work is performed satisfactorily.

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

3

Major Milestones of the Project

- | | |
|------------------|---|
| • January 2001 | Proposals Submitted |
| • May 2002 | PwC revised proposal submitted |
| • June 2004 | Contract signed with PwC |
| • August 2004 | First meeting with all parties |
| • September 2004 | First surveys sent out |
| • January 2005 | Survey closed |
| • March 2005 | Survey reopened to top 50 retailers |
| • April 2005 | Survey closed |
| • October 2005 | Data entry, cleanup, imputations, weighting and tabulations completed |
| • December 2005 | First draft of Phase I distributed |
| • January 2006 | Second meeting with all parties |
| • April 2006 | Revised draft of Phase I submitted |

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

4

Joint Cost of Collection Study: What Is It?

- Stratified sample of retailers by:
 1. Size (annual sales)
 2. State ranked by complexity of sales/use tax
 3. SIC Code
- Goals:
 1. Estimate sales tax compliance cost of retailers in collecting tax from customer under existing state laws. Study does not estimate compliance costs of retailers for use tax on their purchases
 2. Estimate how state policies affect compliance costs
 3. Estimate how characteristics of retailers affect compliance
 4. Project how Streamlined Sales Tax would affect compliance costs

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

5

Joint Cost of Collection Study: What Is It?

Definition and Measurement of Compliance Costs

- Study estimates *incremental* costs of compliance – costs incurred by retailers *over and above* costs that would be incurred if no sales tax
 1. Internal personnel costs
 2. Internal non-personnel costs
 3. External costs
- Transfers included in to obtain estimates of *net* costs
 1. Vendor discounts
 2. “Float”

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

6

Sales Tax Compliance Costs

Retailer Compliance Activities

- Training personnel
- Programming cash registers and other systems
- Documenting exempt sales
- Audits and appeals
- Other data collection and records retention
- Preparing forms, collecting and remitting tax

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

7

Sales Tax Compliance Costs

State Policies Affecting Compliance Costs

- Number and types of statutory exemptions
 1. Exemption of goods
 2. Exempt purchasers
 3. Exempt sellers
 4. Exempt uses
- Variation in bases/rates among jurisdictions
- Local administration {affects number of returns filed}
- Treatment of remote sales
- Frequency of audits

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

8

Sales Tax Compliance Costs

Retailer Characteristics

- Type of retailer (SIC Code)
- Number of store in each state
- Gross sales and taxable sales (2003)
- Number and types of full-time equivalent employees
- Exempt sales
- Percent remote sales
- Number of Stock Keeping Units (SKU)

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

9

Joint Cost of Collection Study What Does It Say?

General Results:

- The bigger the business, the lower the compliance cost.
- The more states in which a firm does business, the higher the compliance cost.
- The greater the proportion of direct marketing sales, the higher the compliance cost.
- The more complex the business (measured by number of SKU's) does not necessarily result in higher compliance costs.
- **Compliance costs do not vary directly with complexity of state sales taxes**

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

10

Joint Cost of Collection Study What Does It Say?

Table 1. Gross Compliance Costs by Type and Size of Annual Retail Sales, 2003
As a Percentage of total state and local sales tax collected

Compliance Costs	Annual Retail Sales Size Class (\$000)			
	\$150 - \$1,000	\$1,000 - \$10,000	Over \$10,000	Weighted Average
For retailers that provided cost breakdowns	16.84%	4.21%	1.03%	1.81%
Training of personnel on sales tax	1.87	0.55	0.35	0.71
Documenting tax-exempt sales	3.80	0.87	0.13	0.31
Customer service relating to sales tax issues	0.74	0.21	0.06	0.10
Sales tax related software and license fees	1.86	0.36	0.10	0.17
Programming and servicing cash registers	1.17	0.35	0.10	0.16
Returns, remittances, refund credits, sales tax research	5.35	1.19	0.12	0.38
Dealing with sales tax audits and appeals	1.03	0.46	0.12	0.18
Other compliance costs	1.03	0.23	0.05	0.11
For retailers that did not provide cost breakdowns	9.08%	3.41%	1.54%	2.56%
Related compliance costs for all retailers	1.85%	1.29%	1.02%	1.09%
Debit/credit card fees on sales tax	0.76	0.76	0.64	0.66
Unrecovered sales tax paid due to bad debts	1.09	0.53	0.38	0.43
Total gross compliance costs	13.47%	5.20%	2.17%	3.09%
Net implicit transfers	1.11%	0.82%	0.54%	0.60%
Vendor discounts	0.96	0.68	0.45	0.50
Net float	0.15	0.14	0.09	0.10

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

11

Joint Cost of Collection Study What Does It Say?

Table 2. Gross Compliance Costs by Type and Size of Annual Retail Sales, 2003
As a Percentage of total taxable sales

Compliance Costs	Annual Retail Sales Size Class (\$000)			
	\$150 - \$1,000	\$1,000 - \$10,000	Over \$10,000	Weighted Average
For retailers that provided cost breakdowns	0.83%	0.27%	0.06%	0.11%
Training of personnel on sales tax	0.09	0.03	0.02	0.03
Documenting tax-exempt sales	0.18	0.05	0.01	0.02
Customer service relating to sales tax issues	0.03	0.01	0.00	0.01
Sales tax related software and license fees	0.09	0.02	0.01	0.01
Programming and servicing cash registers	0.06	0.02	0.01	0.01
Returns, remittances, refund credits, sales tax research	0.25	0.08	0.01	0.02
Dealing with sales tax audits and appeals	0.06	0.01	0.00	0.01
Other compliance costs	0.06	0.01	0.00	0.01
For retailers that did not provide cost breakdowns	0.55%	0.20%	0.90%	0.15%
Related compliance costs for all retailers	0.11%	0.08%	0.06%	0.07%
Debit/credit card fees on sales tax	0.05	0.05	0.04	0.04
Unrecovered sales tax paid due to bad debts	0.07	0.03	0.02	0.03
Total gross compliance costs	0.82%	0.32%	0.13%	0.19%
Net implicit transfers	0.07%	0.05%	0.00%	0.04%
Vendor discounts	0.06	0.04	0.03	0.03
Net float	0.01	0.01	0.01	0.01

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

12

Joint Cost of Collection Study What Does It Say?

Table 3. Gross Compliance Costs by Type of Retailer and Size of Annual Retail Sales, 2003

Type of Retailer	Annual Retail Sales Size Class (\$000)							
	\$150 - \$1,000		\$1,000 - \$10,000		Over \$10,000		Weighted Average	
	As Percent of		As Percent of		As Percent of		As Percent of	
	Total State and Local Sales Tax Collected	Total Annual Sales	Total State and Local Sales Tax Collected	Total Annual Sales	Total State and Local Sales Tax Collected	Total Annual Sales	Total State and Local Sales Tax Collected	Total Annual Sales
Total gross compliance costs	13.47%	0.82%	5.20%	0.32%	2.17%	0.13%	3.09%	0.19%
Number of nexus states*	13.47%	0.82%	5.07%	0.31%	2.15%	0.13%	3.06%	0.19%
One	13.50%	0.82%	5.02%	0.31%	3.65%	0.18%	6.17%	0.34%
Two to Four	(D)	(D)	3.47	0.20	1.42	0.08	1.59	0.31
Five to Nine	No observations		(D)	(D)	1.33	0.09	1.80	0.10
Ten or More	No observations		No observations		1.94	0.13	1.94	0.17
Percent of Direct Market Sales*	13.47%	0.82%	5.20%	0.32%	2.17%	0.13%	3.09%	0.19%
Exactly 0%	13.02	0.80	5.13	0.31	2.22	0.13	3.95	0.66
Between 0% and 90%	14.83	0.89	4.71	0.31	2.1	0.13	2.39	0.43
Above 90%	(D)	(D)	10.68	0.52	4.85	0.30	7.60	0.03
Taxable sales as percent of all sales*	13.47%	0.82%	5.20%	0.32%	2.17%	0.13%	3.09%	0.19%
Less than or equal to 25%	46.24	3.64	11.69	1.05	8.07	0.56	12.24	0.91
Between 25% and 100%	11.21	0.74	5.13	0.32	2.13	0.13	2.79	0.17
Exactly 100%	15.50	0.82	4.10	0.23	1.90	0.12	3.70	0.23

* Weighted average of observations.

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

13

Joint Cost of Collection Study What Does It Say?

Table 4. Gross Compliance Costs by Number of SKU's and Volume of Retail Sales

	Annual Retail Sales (\$000)							
	\$150-\$1,000		\$1,000 - \$10,000		Over \$10,000		Weighted Average	
	Percent of Tax Collected	Percent of Taxable Sales	Percent of Tax Collected	Percent of Taxable Sales	Percent of Tax Collected	Percent of Taxable Sales	Percent of Tax Collected	Percent of Taxable Sales
< 1	11.0	0.7	5.1	0.3	3.1	0.1	5.9	0.3
1 - 5	13.6	1.0	4.2	0.3	3.8	0.2	5.8	0.4
5 - 10	34.9	1.0	10.1	0.6	2.3	0.2	3.1	0.2
10 - 25	16.8	1.0	6.3	0.4	1.3	0.1	2.2	0.1
25 -50	(D)	(D)	3.2	0.2	2.3	0.1	2.8	0.2
50 - 100	(D)	(D)	3.8	0.2	1.6	0.1	1.8	0.1
> 100	(D)	(D)	(D)	(D)	2.2	0.1	2.3	0.1
Weighted Average	13.5	0.8	5.2	0.3	2.2	0.1	3.1	0.2

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

14

Joint Cost of Collection Study What Does It Say?

**Table 5. Gross Compliance Costs by Type of State and Size of Annual Retail Sales, 2003
Single State Retailers Only**

State Group	Annual Retail Sales Size Class (\$000)							
	\$150 - \$1,000		\$1,000 - \$10,000		Over \$10,000		Weighted Average	
	As Percent of		As Percent of		As Percent of		As Percent of	
	Total State and Local Sales Tax Collected	Total Annual Sales	Total State and Local Sales Tax Collected	Total Annual Sales	Total State and Local Sales Tax Collected	Total Annual Sales	Total State and Local Sales Tax Collected	Total Annual Sales
1	19.38%	1.07%	5.63%	0.31%	7.74%	0.25%	9.13%	0.38%
2	19.80	1.30	4.14	0.23	8.19	0.27	8.90	0.43
3	10.57	0.50	2.74	0.14	2.36	0.07	5.01	0.20
4	9.90	0.72	4.30	0.29	2.13	0.10	4.54	0.26
5	19.93	1.43	7.67	0.42	1.60	0.09	8.23	0.49
6	10.83	0.87	5.63	0.37	1.87	0.14	4.48	0.34
7	20.10	0.53	6.71	0.47	1.59	0.12	5.52	0.34
8	(D)	(D)	3.70	0.19	3.63	0.13	4.26	0.18
9	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Weighted Average	14.24%	0.86%	5.36%	0.31%	3.19%	0.15%	6.19%	0.33%

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

15

Joint Cost of Collection Study What Does It Say?

Table 6 State Groupings

State Group	Characteristics of State Tax	States
1	No Local Sales Taxes	CCT, DC, HI, IN, KY, ME, MS, NJ, RI, WV
2	Uniform base and rate, origin based, state administered	PA, VT, VA
3	Uniform base, destination based, state administered	IA, MN, NC, WI
4	Uniform base among locals, state/local base conformity, origin based, state administered	AR, IL, MO, NM, OH, TN, TX, UT, WA
5	Uniform base among locals, state/local base conformity, variable rates, destination based, state administered	FL, KS, NE, NV, OK, WY

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

16

Joint Cost of Collection Study What Does It Say?

Table 6 State Groupings, Continued

State Group	Characteristics of State Tax	States
6	Uniform rates/bases among locals, state/local base variation, variable rates, destination based, state administered	CA, GA, SD
7	Variable rates/bases among locals, variable state/local bases, destination based, state administered	ND, NY, SC
8	Variable rates/bases among locals, variable state/local bases, destination based, locally administered	AL, AK, AZ, CO, ID, LA
9	No Sales Tax	DE, MT, NH, OR

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

17

Joint Cost of Collection Study What Does It Say?

Summary & Conclusions

- Phase I was only the data gathering stage
- Crosstab analysis indicates what elements of retailers' costs would *probably* be the "drivers:"
 1. Personnel training
 2. Tax exemptions
 3. Possibly no. of SKU's and proportion of direct sales

June 7, 2006

JCCS Federation of Tax Administrators Annual Meeting

18

Joint Cost of Collection Study What Does It Say?

Summary & Conclusions

- Phase II – the econometric analysis will provide more definitive answers regarding cost drivers
- Results from Phase II of JCCS will provide answers to how much of the compliance costs will be shifted from retailers to SSTP.