

Resolution 2010 - 1

State Sales Tax Simplification and Fairness Policy

Background

The U.S. Supreme Court held in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992) that a state may not require a seller that does not have a physical presence in the state to collect sales or use tax on sales into the state. The decision was based in part on the complexity of the sales tax system for remote sellers (nonresident sellers without a physical presence in the state of purchase). The Court also said clearly that Congress could authorize states to require remote sellers to collect tax.

Since the *Quill* decision, online retailing and remote sales have exploded as the Internet has become the preferred way of doing business for many Americans. According to the US. Department of Commerce, Internet retail sales grew more than 14 percent during the first quarter of 2010 while total retail sales grew by only 6 percent.

To address the issue of complexity for multistate sellers, states have worked closely with the business community for more than eight years to simplify administration of sales and use taxes for fixed-base retailers as well as for remote sellers. A major goal of the Streamlined Sales Tax Project was to reduce the compliance burden for multistate sellers.

The Project created the Streamlined Sales and Use Tax Agreement. The Agreement sets out sales tax simplifications states must adopt in order to be members of the Streamlined Sales Tax Governing Board. The Agreement was created in November 2003 and became effective on October 1, 2005, when the requisite number of states simplified their sales and use taxes in accordance with the requirements of the Agreement. At the present time, there are 20 full member states and three associate member states. More than 1,000 sellers have voluntarily registered to collect tax under the Agreement. Key simplifications addressed by the Agreement include state-level administration of all local sales taxes, greater use of technology, safe harbors for sellers, and uniform definitions.

Policy

The Federation of Tax Administrators (FTA) finds the ability to require remote sellers to collect sales and use taxes on goods and services sold into a state to be of the highest importance. As such, FTA supports the enactment of federal legislation that would authorize members of the Streamlined Sales and Use Tax Agreement to require remote sellers to collect sales and use taxes on goods and services sold into the state. A significant number of states have simplified their sales taxes and it is time for Congress to act on remote sales legislation. Any such federal legislation should reflect the actual policies of the Streamlined Sales and Use Tax Agreement and should not condition the grant of authority on compliance with requirements not in the Agreement. Remote sales legislation should be self-activating and not require additional federal authorizations or rulemaking, and it should respect the authority of the states to govern the affairs of the Agreement. FTA believes it is appropriate that certain remote sellers with a limited sales volume be exempted from the collection requirement. Federal legislation should not incorporate any language that limits state taxing authority.

This resolution shall automatically terminate three years after the Annual Business Meeting at which it is adopted, unless reaffirmed in the normal policy process. Adopted by the Annual Meeting of the membership June 9, 2010.

Passed unanimously by voice vote during the business meeting on June 9, 2010

Resolution 2010-2
Expanding Federal Refund Offset for State Tax Debts

Background

The U.S. Treasury Department's Financial Management Service offsets federal tax refunds and other government payments for a variety of debts owed the federal government, including child support, student loans and federal tax delinquencies. The IRS Restructuring Act of 1998 (P.L. 105-206) authorized states to join the federal Tax Offset Program. Current law allows states to use the federal offset program to collect their delinquent income tax debts, but from resident taxpayers only (defined as a taxpayer whose address on the federal return is in that state). The restriction was intended to give the program time to prove itself to be effective and non-controversial. Each year states collect more than \$200 million in delinquent tax debts from this program.

The program contains a series of safeguards to insure that residents and nonresidents alike receive adequate notice of the debt that is due and that further inaction will result in the debt being referred to offset. Financial Management Service estimates that states should be able to collect more than \$80 million each year if offsets are allowed from nonresident debtors. Provisions that would have expanded the federal refund offset program to include the debts of nonresident state taxpayers were included in two bills in the 109th Congress, but did not make it to final passage. The provision is not considered controversial.

The Financial Management Service and Treasury Department support expansion of the tax offset program. Increasing the volume of debt the federal government collects permits greater administrative efficiencies through economies of scale. Also, the states pay a fee for each successful offset, which covers the federal government's fully loaded share of the cost of the federal offset program. In the 111th Congress a bill (H.R. 2303) to expand the Program was introduced by Rep. John Lewis (D-GA), the Chairman of the IRS Oversight Subcommittee of the House Ways and Means Committee.

Policy

The Federation of Tax Administrators supports expanding the federal Tax Offset Program to include income tax debts owed by all taxpayers, not just state residents.

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Resolution 2010-3
Federal Preemption of State Property Tax Authority

Background

In 1976, Congress passed the Railroad Revitalization and Regulatory Reform Act (the “4-R Act”), which prohibits states and local governments from taxing railroad property at higher rates or ratios of value than those for other commercial and industrial property. It also provides that railroads may pursue claims under the Act in federal court.

Similar, but not identical, protections have also been accorded the interstate airline and motor carrier industries.

From the states’ perspective, the 4-R Act and its progeny have had a number of undesirable effects on state and local property tax systems. Thirty years of litigation still has not fully defined the contours of the 4-R Act.

Contentious litigation was repeated in many states over the identification of which commercial and industrial property taxes constituted the comparison class for railroads, the jurisdiction and role of the federal courts, what taxes besides property taxes were included and how to deal with exempt property.

Beyond the litigation, 4-R Act-like protections have disrupted state property tax systems. This is particularly true in states that have a constitutional system that allows for different classes of property. Such protections have also established a preferred class of taxpayer and they lead to requests for similar treatment by additional industries. The scope of the 4-R preemption vastly exceeds the original stated Congressional intentions because the “any other tax” provisions in the Act have been construed to apply to other taxes besides property taxes.

There have been a variety of state tax restrictions proposed for different types of property or activities that are similar to the 4-R “non discriminatory” prohibitions. Proposals have been made for wireless communications, telecommunications companies, interstate natural gas pipelines, hotel reservation businesses and auto rental companies. Extending these provisions to other industries could cause serious and widespread revenue consequences to the states and localities. The most dramatic impact will be felt in those states where the voters have approved a constitutional amendment authorizing differential treatment of certain types of taxpayers. In effect, Congress will be substituting its judgment for the judgment of state voters.

Policy

The Federation of Tax Administrators strongly opposes action by Congress and federal agencies that would abrogate, disrupt or otherwise restrict states from imposing taxes that are otherwise lawful under the U.S. Constitution or from effectively administering those taxes. FTA believes Congress should undertake an active program of consultation with states as it considers measures that would preempt state tax authority.

FTA strongly opposes prohibitions of state taxing authority on the types or level of taxes that states can impose, including the establishment of property tax rates and classes. Decisions about property tax assessments, rates and policies and property tax administration should be left to state and local elected officials and the citizens they represent.

Congress should respect the states’ administrative and judicial processes for dealing with tax appeals, which are the appropriate means to protect taxpayers from unconstitutional discrimination.

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Resolution 2010-4

Business Activity Tax Nexus Legislation

Background

Business activity taxes are levied by states for the privilege of doing business in or earning income within a state. These include state corporate income taxes, gross receipts taxes, business license taxes, franchise taxes, business and occupation taxes, and insurance premiums taxes.

Decisions by the U.S. Supreme Court allow a state to tax business activities within the state if there is a substantial nexus between a commercial entity doing business in the state and the taxing state. A number of state courts have held that the taxed entity need not have a physical presence in the taxing jurisdiction in order to be subject to a business activity tax, and the Supreme Court has specifically stated that it has not applied a physical presence requirement to the imposition of business activity taxes.

In the 111th Congress, a Business Activity Tax Simplification Act (H.R. 1083) was introduced. No Senate version of the bill has been introduced in this Congress unlike in past years when Senate versions of the legislation were introduced. The bill would eliminate state jurisdiction to tax businesses that have no physical presence in the state, and provide that certain types of physical presence would not be considered for purposes of determining the jurisdiction to impose business activity taxes. The bill also would expand P.L. 86-272 to all forms of business activity taxes (instead of just net income taxes) and to the solicitation of sales of all types of property and services instead of just tangible personal property.

State tax agencies and other officials resisted enactment of legislation such as H.R. 1083 and other similar bills in past Congresses for several reasons:

- The legislation represents a break from existing U.S. Supreme Court precedent and is a substantial reversal of current law.
- The legislation would allow many companies to engage in tax planning and structuring in order to avoid substantial amounts of tax in their domicile state and the states in which they do business essentially changing their business form, but not the nature of the income-producing activities. In particular, larger companies would be able to transfer intangible assets to holding companies incorporated in no-tax or low-tax states.
- The legislation would impose the largest unfunded tax preemption mandate ever estimated by the U.S. Congressional Budget Office, a state revenue loss of \$3 billion per year within three years.
- The legislation favors out-of-state businesses over in-state businesses. It would allow a large corporation that can conduct business online to go into a state electronically and exploit the market in that state without being subject to the taxes that in-state businesses are required to pay.
- The expansion of P.L. 86-272 is unwarranted and runs counter to the direction that business operations are taking.

Policy

The Federation of Tax Administrators strongly opposes any legislation that would restrict a state's constitutional authority to tax entities doing business in a state. FTA opposes any legislation that would establish a physical presence nexus requirement for the imposition of state business activity taxes.

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Resolution 2010-5

Preemption of State and Local Authority to Tax

Background

The power to define the state and local tax system is a core element of state sovereignty, and the United States Constitution establishes the boundaries of the sovereignty of the states in the tax arena. The system of federalism that is defined by the United States Constitution further assigns to state and local governments the responsibility for supplying the majority of the daily services due to its citizens and residents. A vibrant state and local tax system is essential to meeting those needs, and the United States government has traditionally shown substantial deference to the tax sovereignty of the states

An increasing number of groups seek to preempt state taxation authority in particular areas for a variety of reasons. Beyond the opposition to the incursion on state sovereignty, states have also generally resisted federal preemption efforts because preemption of state tax authority has the effect of establishing a preferred class of taxpayers and shifting the tax burden to other non-preferred taxpayers. Moreover, such preemptions often have unintended consequences that work significant disruptions of state and local tax systems.

Our system of federalism can result in substantial administrative compliance burdens for persons with tax responsibilities in multiple states. Many of the legitimate goals that might be pursued in preemptive legislation can be effectively achieved through cooperative state efforts and improved uniformity among the states. States have an obligation to pursue such efforts.

Policy

The Federation of Tax Administrators strongly opposes action by Congress and federal agencies that would abrogate, disrupt or otherwise restrict states from imposing taxes that are otherwise lawful under the U.S. Constitution or from effectively administering those taxes. FTA believes Congress should undertake an active program of consultation with states as it considers measures that would preempt state tax authority. Finally, states should actively pursue such uniformity and simplification measures as are necessary and effective to address concerns of administrative burden in complying with the tax laws of multiple states.

While federal preemption is generally to be resisted, preemptive legislation can, at times, promote simplification, uniformity, and taxpayer compliance, albeit at some cost to state sovereignty. FTA will evaluate proposed federal legislation that preempts state taxing authority against several criteria. (1) Recognizing that the benefits of federalism will impose administrative burdens on commerce, is there disinterested evidence that the administrative burden and complexity posed by current state and local practices is impeding the growth of commerce? (2) Does the proposed preemption address issues of simplification and complexity? (3) Can meaningful simplifications and uniformity be achieved through state action without preemption? (4) Would preemption disrupt state and local revenue flows and tax systems? (5) Would preemption cause similarly situated taxpayers to be taxed differently; specifically, does the proposal create advantages for multistate and multinational businesses over local business? (6) Does the preemption support sound tax policy? (7) Does the preemption create unknown or potential unintended consequences? (8) Have state tax authorities and taxpayer representatives together agreed to a beneficial change in federal law?

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Resolution 2010-6

Extension of the Internet Tax Freedom Act

Background

In 1998 Congress enacted the Internet Tax Freedom Act, which placed a moratorium on new or increased state and local taxes on charges for Internet access and prohibited “multiple and discriminatory” taxes on electronic commerce.

The temporary moratorium has been extended three times. In 2004, the Act was expanded to preempt state and local taxation of purchases of telecommunications services that are “purchased, used, or sold by a provider of Internet access to provide Internet access.” In 2007, the Act was extended again until November 1, 2014.

Nine states currently impose transaction taxes on charges for Internet access. These taxes are allowed under a “grandfather” clause authorizing such taxes if they were in place prior to 1998; that “grandfather” protection also will expire in November 2014.

The “grandfather” provision covers all “taxes on Internet access” which is a defined term that means any tax on Internet access services or providers of Internet access – other than net income, property, and franchise taxes. The 2007 Act, clarified that a “tax on Internet access” did not include a “State tax expressly levied on commercial activity, modified gross receipts, taxable margin, or gross income of the business enacted under specified terms.” That said, the grandfather provision may still apply to an unknown number of state and local gross receipts or other general purpose transaction taxes that are levied against Internet service providers that are not covered by the 2007 Act’s clarification. If the moratorium is made permanent without a grandfathering clause it is possible that taxpayers will challenge the imposition of many indirect taxes that apply to Internet Access. Bills have been introduced in the 111th Congress (H.R. 1560 and S. 43) to make the Act permanent and to repeal the grandfather clause.

The Government Accountability Office has reported that there is no statistically significant relationship between state taxation of charges for Internet access and the adoption of broadband by users or the deployment of broadband by providers.¹ This means the moratorium is not effective in achieving its purported purpose of expanding the availability of Internet access to the American public. A study by economists at the University of Tennessee produced similar results, finding that other issues (e.g., household income and educational levels) were more important in the proportion of a state’s population that had access to the Internet than whether the state imposed tax on access charges.²

In 2010, class action suits were filed in a number of jurisdictions challenging taxes collected by AT&T Mobility Wireless Data Services as being prohibited by the Act. That litigation is likely to test the scope of the Act and whether it applies to particular state and local taxes and fees, threatening substantial negative impacts on state and local governments.

¹ Government Accountability Office, “Telecommunications – Broadband Deployment is Extensive throughout the United States, but It Is Difficult to Assess the Extent of Deployment Gaps in Rural Areas” (GAO-06-426). In the GAO study, the term “deployment” refers to the offering of broadband services by various types of providers and the term “adoption” refers to the use of broadband services by consumers.

² Donald Bruce, John Deskins and William F. Fox, “Has Internet Access Taxation Affected Internet Use,” *State Tax Notes*, May 17, 2004, pp. 519-526.

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(continued)

Resolution 2010-6

Extension of the Internet Tax Freedom Act

In previous discussions of the legislation, states have argued: (a) The current definition of Internet access should be narrowed to remove the possibility that Internet Service Providers could bundle a wide range of digital products and services with access and claim exemption for the entire bundle; (b) Any extension should be temporary to insure that Congress periodically evaluates the impact of the Act; and (c) The grandfather protection for pre-1998 taxes should be retained to avoid a disruption of the revenue flows of the states involved and to avoid unintended preemptions of taxes covered by the current definition of “tax on Internet access.”

Policy

The Act should be repealed and should not be extended or made permanent. If the Act is not repealed, the definition of “Internet access” should be rewritten so as to eliminate the possibility that certain products and services could be bundled with Internet access and claimed as exempt Internet access.

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Resolution 2010-7

Hotel Tax Preemption

Background

Online Travel Companies (OTCs) like Expedia, Travelocity, Orbitz, Priceline, and Hotels.com, have adopted similar business operating models under which they contract with hotels related to the sale of hotel rooms over the telephone and Internet. OTCs pay discounted rates to hotels that are not disclosed to consumers. The OTCs charge consumers a marked-up retail rate (retail rate) for the accommodations. They also typically charge consumers a processing fee. OTCs collect hotel taxes based on the discounted rate for remittance to state and local taxing authorities.

Hotel taxes have been imposed for more than 30 years. They are collected from consumers and paid over to local and state governments, regardless of how the hotel room is rented, whether over the phone, in person at a hotel, by a travel agent, or on the Internet.

The OTCs' failure to collect hotel taxes on the retail rate hurts tourism in many state and local jurisdictions. Many local hotel taxes are dedicated to funding tourism costs such as hotel to convention center transportation, convention centers, and visitor centers, and historic restoration projects. Education, fire, police and health care budgets also could be reduced.

State and local governments have initiated collection actions against OTCs to compel the remittance of hotel occupancy taxes on the room rate charged to the consumer (the retail price, not the discounted rate). More than 40 court cases are pending nationwide. The number of administrative collection efforts is not known because of confidentiality rules.

OTCs have made several attempts to secure special Federal legislation preempting state and local jurisdictions' taxing authority by prohibiting them from requiring the OTCs to collect hotel taxes on retail rate charged to consumers. This could significantly reduce the hotel occupancy taxes collected when a consumer books a room through an OTC or travel agency. If successful, this legislation could force hotels to try to set up similar booking companies.

Policy

Congress should refrain from enacting any legislation that would restrict the ability of state and local governments from collecting hotel taxes, e.g. occupancy and/or sales taxes, on the full rental price that hotel occupants pay when renting rooms from hotels, travel agents, or OTCs.

This resolution shall automatically terminate three years after the Annual Business Meeting at which it is adopted, unless reaffirmed in the normal policy process. Adopted by the Annual Meeting of the membership June 9, 2010.

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