SUPPORT LOCAL ECONOMIES BY ALLOWING THE COLLECTION OF EXISTING SALES TAXES ON OUT-OF-STATE CATALOG AND ONLINE SALES

QUICK FACTS

- MFA/RTPA is not a new tax. It would allow state and local governments to collect existing sales and use taxes on remote sales
- MFA/RTPA would enable state and local governments to collect sales taxes that are already owed each year that could be dedicated to providing important local services such as infrastructure, public safety, education and economic development
- Passing federal legislation would level the playing field for local retailers who are at a competitive disadvantage to online retailers who do not have to collect taxes

ACTION NEEDED:

Contact your House and Senate members and urge them to support legislation that would allow counties to enforce their existing sales tax laws regardless of whether a purchase is made in a store, online or through a catalog retailer.

BACKGROUND:

The 1967 Supreme Court case National Bellas Hess v. Illinois Department of Revenue set the stage for the current debate on taxing Internet sales. In that case, the Court ruled it would be too much of a burden on out-of-state retailers to collect sales taxes in all the jurisdictions in which they conduct business. In 1992, the issue resurfaced in Quill v. North Dakota, in which the Court reaffirmed Bellas Hess, but elaborated that Congress ultimately has the power to resolve the question of taxation on interstate commerce.

Since those earlier decisions, the Internet’s use and utility has developed tremendously. Consequently, online sales have also grown exponentially in the last fifteen years and are projected to continue to increase. Since state and local governments are still unable to enforce their existing sales tax laws on many of those purchases, billions of local tax dollars are lost each year.

For counties, that increasing level of lost revenue means less money for basic services, such as roads and law enforcement officers. With local economies still recovering from the Great Recession, additional revenue will bolster any recovery efforts, and capturing these revenues is crucial to counties, especially for mandated yet underfunded services.

A bipartisan, bicameral bill was introduced on this issue for the first time in the 113th Congress. The Marketplace Fairness Act of 2013 (S. 336 and H.R. 684) sought to grant state and local governments the authority to collect taxes on remote sales, which generally are sales that are conducted through any means other than in a physical store. On May 7, 2013, the U.S. Senate passed S.336 with bipartisan support (69-27). The efforts were led by Sen. Michael Enzi (R-Wyo.), Sen. Richard Durbin (D-Ill.), Sen. Lamar Alexander (R-Tenn.) and Sen. Heidi Heitkamp (D-N.D.).

Reps. Steve Womack (R-Ark.) and Jackie Speier (D-Calif.) led efforts to pass the bill in the U.S. House, where the measure was referred to the House Judiciary Committee. In September of 2013, Judiciary Chair Bob Goodlatte (R-Va.) released seven principles on Internet sales tax to guide the discussion around the issue. The principles signaled the Chairman’s intent to address the issue and potentially move legislation through the committee. Additionally, the Judiciary Committee conducted a hearing in March of 2014 to explore alternatives to the Senate-passed version of the Marketplace Fairness Act. Unfortunately, the 113th Congress ended with no action from the House on the Senate-passed bill.
The Senate-passed legislation, if it were enacted, would have created two systems to facilitate multistate sales tax collection: the Streamlined Sales and Use Tax Agreement and an alternative in which states would collect taxes after adopting minimum simplification requirements for their sales tax laws and administration. The Streamlined Sales and Use Tax Agreement, supported by NACo and other state and local government organizations, is a multistate compact that seeks to reduce the complexity of state and local sales and use tax laws and would permit the collection of sales and use taxes from remote sellers. Although currently only 24 states are official members of the Agreement, many other states, as well as the District of Columbia, local governments and the business community, were involved in the cooperative efforts to simplify sales and use tax collection that led to the establishment of the Agreement.

The Agreement minimizes costs and administrative burdens on retailers that collect sales tax, particularly retailers operating in multiple states. It encourages remote sellers using the Internet and mail order to collect taxes on sales to customers living in the 24 member states and levels the playing field so that local stores and remote sellers operate under the same rules. The Agreement ensures that all retailers can conduct their business in a fair, competitive environment.

For the 114th Congress, the previously passed version of the Marketplace Fairness Act was reintroduced in the Senate, S. 698, but did not see committee action.

In the House of Representatives, Chairman Goodlatte circulated a discussion draft for his approach to resolving the remote sales tax issue. He was joined by Rep. Anna Eshoo (D-Calif.) in promoting the draft. Their concept took a slightly different approach than legislation introduced in the past by adopting a hybrid version of source sourcing. Under this method, the tax on a remote sale would be based on where an item is sold and not where the customer who bought the item lives. Thus, the method is in contrast to prior legislative proposals and the Streamline Agreement in that the tax collected by the customer’s home jurisdiction would be based on the rate of the remote seller’s jurisdiction. NACo currently does not have a position on the draft and the timeline for bill introduction and any potential committee hearings remains uncertain.

In an interesting and positive development during the 114th Congress, Judiciary Committee member Rep. Jason Chaffetz (R-Utah) introduced H.R. 2775, the Remote Transactions Parity Act of 2015 (RTPA). The bill essentially mirrors the Marketplace Fairness Act in many aspects, such as utilizing destination based sourcing for taxing sales and adopting the two simplification options for states that wish to exercise collection authority. There are some differences between RTPA and MFA and it is currently undetermined how the sponsors would resolve them.

Here are a few notable differences within the RTPA:

- The small seller exception (the threshold of gross annual sales under which a remote seller would not be required to collect) starts at $10 million in the first year, it goes to $5 million in the second year and it finishes at $1 million in the third year after enactment. In the fourth and subsequent years, there is no small seller exception. The MFA establishes a permanent exception at $1 million.

- Additional protections for remote sellers are included: states would need to certify multiple software providers so that remote sellers would be able to use the software of their choice, states would need to provide centralized registration so that remote sellers would not have to repeat the process, and states would not be allowed to audit remote sellers with gross annual sales below $5 million unless there is suspected fraud.

- The most significant difference is the inclusion of language for the definition of a remote seller that comes from legislation NACo opposes, the Business Activity Tax Simplification Act. Specifically, the RTPA establishes an exception for any seller that has an in-state physical presence for less than 15 days to conduct limited or transient business activity. This would run contrary to many state established nexus standards.
In August 2016, Chairman Goodlatte released another discussion draft of his proposed legislation to address the issue – the Online Sales Simplification Act of 2015 (OSSA). This was another positive development and a potential signal that the Chairman might be ready to move some form of legislation in his committee. However, the discussion draft substantially diverged from previous remote sales tax legislation that NACo has supported (i.e. Marketplace Fairness Act (S.698) led by Sens. Enzi (R-Wyo.), Durbin (D-Ill.), Alexander (R-Tenn.), Heitkamp (D-N.D.); and the Remote Transactions Parity Act (H.R. 2775) led by Rep. Jason Chaffetz (R-Utah)).

Most notably, OSSA utilizes a hybrid-origin system to determine the tax on a remote sale. Previous NACo-supported legislation and the Senate-passed version of Marketplace Fairness in 2013 utilize a destination-based system to source the sale. Destination-based means that whether a remote sale is taxable and the applicable rate are both determined by the customer’s home state. Under the hybrid-origin system, the tax base of the seller’s state is coupled with the tax rate of the buyer’s state to determine the tax applicable to the remote sale. This introduces a system that has not previously been put into practice in the retail world.

The second most notable difference in OSSA is that states would be required to adopt a single statewide tax rate for remote sales. Thus, states would no longer be able to allow local governments to “piggyback” on top of the state sales tax. This essentially prevents local governments from deciding their own sales tax policy. In theory, depending on the state, counties may experience an increase or decrease in tax collections based on the rate that would be adopted.

Unfortunately, despite much discussion on remote sales tax issues, the 114th Congress came to an end with no action in the Senate, and in the House, efforts by Chairman Goodlatte and Republican supporters of remote sales tax legislation to find some form of compromise between the various legislative approaches were largely left unresolved.

While it remains undetermined if legislation in the 115th will be reintroduced, adding to the complexity of the issue is that several states are taking steps on their own in the absence of federal legislation. States like South Dakota and Alabama enacted legislation that would require remote sellers to collect sales taxes if they generate over a statutorily set threshold of remote sales in a given year into the state. In other words, even if the remote seller does not have a physical presence in the state, they would be required to collect sales tax as a result of the amount of revenue they are generating in sales within the state.

As expected, lawsuits have already been filed by certain businesses challenging the validity of the laws. For the most part, the states are passing the laws with the intention of generating litigation, with the hopes that the cases would go all the way to the U.S. Supreme Court and provide the Justices with an opportunity to reverse the decision in Quill v. North Dakota, 504 U.S. 298 (1992). Quill upheld the physical presence standard and resulted in the current status quo remote sales tax. Marketplace Fairness supporters were encouraged in 2015 when Justice Kennedy wrote a concurring opinion in Direct Marketing Association v. Brohl,135 S. Ct. 1124, 1135 (2015) in which he argued that given the evolution of technology, it is likely time for the Court to revisit the physical presence standard upheld in the Quill decision.

In 2017, several more states are expected to consider similar legislation.

**KEY TALKING POINTS**

- Members of Congress should support legislative initiatives that would allow states and local governments to enforce existing laws and stop the loss of billions of dollars in uncollected tax revenue on sales in e-commerce every year. This lost revenue will continue growing as e-commerce sales continue to experience significant growth. For example, total online sales for Black Friday 2015 reached over $2.7 billion, a 14 percent increase over the same period in 2014.
• The argument that requiring remote sellers to collect sales tax creates too much of a burden on business are less persuasive today. The retail world is much different today than when the U.S. Supreme Court made its rulings in 1967 and again in 1992. Certified providers with the necessary software to keep track of the various state and local tax rates already exist. Keeping track of tax rates is no more complicated than calculating real-time-shipping, a feature that already exists on most web sites and online sales marketplaces.

• Passing federal legislation on remote sales tax would not add to the federal deficit and does not create a new tax. Federal legislation would also level the playing field for local retailers who are at a competitive disadvantage to online retailers who do not have to collect taxes.

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