SUMMARY AND ANALYSIS OF THE STREAMLINED SALES TAX PROJECT

June 2001

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STREAMLINED SALES TAX PROJECT [http://www.geocities.com/streamlined2000/]

Overview

The Streamlined Sales Tax Project (SSTP) stems from the simplification suggestions made in the minority report of the federal Advisory Commission on E-Commerce (formed by the Internet Tax Freedom Act) and suggestions of the National Governors Association (NGA) in 1999. A group of representatives from over 35 states met throughout 2000 to create a Model Act and Agreement for a uniform sales and use tax act. The language was approved by the participating states in December 2000. While some additional work is needed to fill in some missing pieces, many states will review the Model Act and Agreement to see if they want to adopt the uniform rules. A few states, such as Kansas, have already introduced legislation, and one state – Wyoming, has already enacted legislation. In addition, multistate vendors will also review the SSTP proposal to understand what it might mean for them should states in which they have customers (whether or not the vendor has nexus (taxable presence) in the state) adopt the SSTP proposal.

- Mission: "The Streamlined Sales Tax Project will develop measures to design, test and implement a sales and use tax system that radically simplifies sales and use taxes." [http://www.geocities.com/streamlined2000/oprules.html]
- Developed by 30 participating states and 9 observer states with input from local governments and businesses.
- Focused on simplification for all types of vendors.
- Provides rules on the following in order to improve administration of the sales and use tax:

  "a. State level administration of sales and use tax collections.

  b. Uniformity in the state and local tax bases.

  c. Central, electronic registration system for all member states.

  d. Simplification of state and local tax rates.

  e. Uniform sourcing rules for all taxable transactions.

  f. Uniform definitions within tax bases.

  g. Simplified administration of exemptions.

  h. Simplified tax returns.

  i. Uniform rules for deductions of bad debts.

  j. Simplification of tax remittances.

h. Protection of consumer privacy."

- Specifies three models for collection:

  Model 1 Seller—Uses a CSP (Certified Service Provider) as its agent to perform all sales and use tax functions. However, Seller is responsible for remitting tax on its own purchases.

  Model 2 Seller—Uses a CAS (Certified Automated System) to perform its sales and use tax functions. However, Seller is responsible for remitting tax on its own purchases.

  Model 3 Seller—Has sales in at least 5 member states, total annual sales of at least $500 million, has a proprietary system to calculate tax due in each jurisdiction, and has entered into a performance agreement with the member states.

  Note: The Agreement implies that other types of sellers exist, such as a "Main Street retailers," who would likely just handle their own sales/use tax compliance, just as they do today.

- States are to pay for the system design – vendors will still have some collection costs, particularly Model 2 and 3 Sellers.

- Uniform definitions of items relevant for determination of a member state's tax base are provided for clothing, clothing accessories or equipment, sport or recreational equipment, protective equipment, food and food ingredients, candy, dietary supplement, soft drinks, food sold through vending machines, prepared food, and sales price.

  To give an example of the detail of these definitions, an analysis of "food" follows. The Model Agreement provides that "food and food ingredients" means "substances, whether in liquid, concentrated, solid, frozen, dried, or dehydrated form, that are sold for ingestion or chewing by humans and are consumed for their taste or nutritional value." "Food and food ingredients" does not include alcoholic beverages or tobacco. The Model Agreement's definition of "candy" is "a preparation of sugar, honey, or other natural or artificial sweeteners in combination with chocolate, fruits, nuts, or other ingredients or flavorings in the form of bars, drops, or pieces. Candy shall not include any preparation containing flour and shall require no refrigeration." Candy can be excluded from the definition of "food and food ingredients." Thus, a member state would be able treat "food and food ingredients" as exempt from sales tax, but tax "candy." Or, both could be subject to tax or exempt. In addition, with "food sold through vending machines" defined separately, "candy" sold via a vending machine could be exempt while "candy" sold via other means could be taxable. There are various combinations possible, provided the member states uses the model uniform definitions. "Soft drinks" are also separately defined from "food" and thus, would have the same tax options as "candy."

  "Sales price" is defined to include seller costs of the property or services sold plus delivery and installation charges, unless separately stated.

  <u>Query</u>: Will states agree with the uniform definitions? To the extent the uniform definitions don't match definitions currently used by a state and the state currently has some exemptions within the uniform definitions, it will likely find that use of the uniform definitions will be a revenue raiser or loser. For example, a few states, such as California, do not apply sales tax to electronically delivered software. Under the Model Agreement, if such items were grouped with other items that California does subject to sales tax, the tax base would increase.

- The Model Agreement does not include a definition for "tangible personal property," a term that is quite important in most states, including California. Under California law, sales tax is imposed on retailers for the privilege of selling tangible personal property. California R&T §6016, defines "tangible personal property" as "personal property which may be seen, weighed, measured, felt, or touched, or which is in any other manner perceptible to the senses." It is likely the SSTP is still working on a definition of "tangible personal property." One important aspect of the definition is whether it includes digital products, such as software transferred electronically, because some states currently treat such items as tangible and others (such as California) do not.

- Tax Rates – One Rate or Multiple Rates: The SSTP proposal does not require one-rate-per-state. Whether Congress will view such omission as sufficient simplification to warrant allowing member states to impose sales tax collection obligations on remote sellers is a debate that will occur as more serious discussion takes place in Congress and the States.

  <u>Analysis</u>: Various proposals have called for simplification to include one-rate-per-state. Examples of such proposals include:

- Senator Bumpers' Consumer and Main Street Protection Act of 1997 (S. 1586, 105th Congress) basically called for one-rate-per-state for remote sales.
- The NGA's proposal "EC-12. Streamlining State Sales Tax Systems" (adopted Winter 1999) called for one-rate-per-state for remote sales and a requirement that states "establish a method of distributing to local governments their appropriate share of such taxes."
- S. 288 (Wyden, 107th Congress) calls for one-rate-per-state for all sales transactions.
- S. 512 (Dorgan, 107th Congress) calls for one-rate-per-state only for remote sales transactions.

Some of the issues surrounding a one-rate-per-state system include:

a. Should the one-rate-per-state apply only for remote sale or for all sales? Arguably, the simplification argument only applies to multistate vendors operating remotely in some states. That is, a Main Street retailer with a store in San Jose (8% rate) and another in San Luis Obispo (7% rate) can easily charge these differing rates in each store. On the other hand, a remote vendor with no physical location in California and selling to individuals in all counties, would face a wider range of rates and, unlike the Main Street retailer, would have to find out from each customer where they live so the proper tax rate could be determined.

   However, if one-rate-per-state only applies to "remote vendors" it remains necessary to have nexus guidelines to assist in determining if a vendor is "remote" or "physically present." This is an issue that results in a fair amount of litigation and confusion.

b. How should a state, such as California with multiple rates, determine what its "one-rate" would be? While a weighted average rate might be determinable that would be revenue neutral looking at all cities and counties as a whole, there would be winners and losers among local jurisdictions in their sales tax collections.

c. Neutrality would not be achieved if "one-rate" only applied to remote vendors. That is, if the tax rate applied by the computer vendor in town is 8.25% and the rate from the remote computer vendor is the state's "one-rate" of 7.25%, a buyer might find it to be a better deal to buy from the remote vendor. Under a neutral tax system, the tax cost should not play a part in this decision as to where to buy a product. Of course, tax principles, such as neutrality, must be weighed against other tax principles, such as simplicity, because it is not always possible to achieve all tax principles that make for an ideal tax system. Some local governments will also have to consider that while one-rate-per-state on remote sales may not generate sales tax at the local jurisdiction's higher established rate, it can though, lead to sales tax collections that otherwise would not have occurred (because use tax compliance, particularly among individual consumers, is almost non-existent).

- The Model Agreement is not effective until adopted by at least five states.

Following approval of the draft Agreement and Act in December 2000 by the states participating in the SSTP, the National Governors Association (NGA) expressed its continued support of the project. In January 2001, the National Conference of State Legislatures (NCSL) voted to approve the SSTP, but with significant amendments. For example, the NCSL removed the uniform definitions. The Appendix to this outline notes the changes made by the NCSL.

The Appendix also compares the simplification proposals of the SSTP to those suggested in S. 288 and S. 512 for a simplified sales and use tax system for remote sales. S. 288 (107th Congress) is Senator Wyden's proposal to extend the federal moratorium of the Internet Tax Freedom Act (ITFA) and to suggest features that must exist for the sales tax to be simplified enough to allow participating states to obtain Congressional approval to collect sales and use tax from remote (non-present) vendors. S. 512 (107th Congress) is Senator Dorgan's bill to extend the ITFA moratorium and state the features of a streamlined sales and use tax system. The Appendix highlights areas where Congress and the states may be in disagreement over what constitutes a simplified sales and use tax system.

California and the SSTP

SB 1949 was introduced in February 2000 by Senators Costa and Chesbro. This bill would have directed the Governor to enter into discussions with other states "regarding the development of a multistate, voluntary, streamlined system for sales and use tax collection and administration." SB 1949 was passed in both the California

Assembly and Senate, but was vetoed by Governor Davis in September 2000 because he deemed it unnecessary. He noted that California already participates in such forums as the Multistate Tax Commission and National Governor's Association that work on tax simplification activities. It is certainly possible, given the fact that the Legislature supported streamlined sales tax efforts, that legislation related to work of the SSTP could be reintroduced in California. In addition, as noted by Governor Davis, simplification work of the MTC and NGA (an organization that supports the SSTP) could lead California to consider all or part of the SSTP proposal.

Considerations for Local Governments

- How much of the administrative costs of the SSTP approach would the states pass along to local jurisdictions?
- Today, the city's share of the sales tax (1¢) is sourced under the origin principle (where the sales office is located, rather than where the product was shipped to). This is different than provided for in the Model Act. Could cities continue to use the origin approach, or would they also have to adopt the sourcing rule of the Model Act? What would be the revenue effect to cities if the sourcing rule were changed (there would be winners and losers)?
- S. 288 calls for one-rate-per state (the SSTP does not). Today, there are 8 different sales tax rates used in California. While one-rate per state would make collection easier for remote vendors, it would be difficult to achieve – there would be winners and losers. Also, the highest rate cannot just be adopted because revenue neutrality would not be achieved.
- Should efforts be made to redefine the tax base in California using the uniform definitions? Should intangibles be subject to tax (such as digitized products)?

THE 107TH CONGRESS

H.R. 2421 (Stearns) **-** proposes an exercise of congressional power under article I, section 8, clause 3 of the Constitution (to regulate commerce) to give sole responsibility and authority to the federal government to regulate digital commercial transactions. This would/could prohibit states from taxing digital commercial transactions.

S. 664 (Gregg) - the "New Economy Tax Fairness Act" or NET FAIR Act provides that no state may assert any business activity tax or impose sales and use tax collection obligations on a vendor that does not have a "substantial physical presence" in the State. The bill provides a list of activities which do not constitute a substantial physical presence. The list of "protected" activities includes solicitation of orders by the vendor or the vendor's representative for the sale of tangible or intangible personal property or services if the orders are approved or rejected outside of the state and approved orders are filled by delivery from a point outside of the State, presence or use of intangibles (such as trademarks or electronic signals or web pages) in the state, use of a web site, and use of an unaffiliated contractor in the state to perform warranty or repair work on property sold by a vendor located outside of the State. The "protections" do not apply to a vendor incorporated in the state or any individual domiciled or a resident of the State. An agency relationship may constitute a "substantial physical presence" in the State. An agency relationship only exists if it "(1) results from the consent by both persons that one person act on behalf and subject to the control of the other; and (2) relates to the activities of the person within the State." The provision is effective upon enactment and so will not invalidate collection of any business activity tax imposed prior to that date (even though it violates one of the "protections'). If a vendor terminates its "substantial physical presence" in the State, the State can no longer after that point impose an obligation to pay a business activity tax or to collect and remit a sales or use tax upon the vendor. S. 664 is identical to S. 2401 introduced by Senator Gregg in the 106th Congress.

Senator Gregg notes: "NET FAIR provides legal certainty for companies and consumers that engage in interstate commerce via the Internet, telephone, or mail order. This bill adheres to our Founding Fathers' tenet of 'no taxation without representation' by codifying fair taxation principles. We cannot stand idly by and allow this new economic avenue to be hampered with new taxes. This legislation does not preempt a State's right to tax commerce; however, it does protect businesses and consumers from unfair taxation on interstate commerce and from what could be a crippling effect on the growth of the new 21st Century economy." [Congressional Record of 3/29/01, S3172]

S. 589 (Smith) - would make the Internet Tax Freedom Act moratorium permanent, but keep the grandfather provision which allows states to impose taxes on Internet access if such taxes were generally imposed and actually enforced prior to October 1, 1998.

H.R. 1552 (Cox) - would extend the ITFA moratorium through the end of 2006. It would also remove the grandfather provision so that no state or local government could impose taxes on Internet access.

S. 777 (Allen) and H.R. 1675 (Cox) - would permanently extend the ITFA moratorium and remove the grandfather provision so that no state or local government could impose taxes on Internet access fees.

S. 512 (Dorgan) and **H.R. 1410** (Istook) – would extend the Internet Freedom Act moratorium on multiple and discriminatory taxes for 4 years (through December 31, 2005) and provide that states that sufficiently simplify their sales/use tax systems may be allowed to collect sales/use tax from remote vendors. S. 512 provides criteria for a simplified sales tax system. The bill also calls upon the States to take the lead in developing and implementing a simplified, non-discriminatory sales tax system. In addition, S. 512 calls for a "joint, comprehensive study ... by State and local governments and the business community to determine the cost to all sellers of collecting and remitting State and local sales and use taxes on sales made by sellers under the law as in effect on the date of enactment of [S. 512] and under the [streamlined sales and use tax system called for in S. 512] to assist in determining what constitutes reasonable compensation." Finally, S. 512 calls for a single uniform statewide use tax rate on all remote sales. See the Appendix for further information.

S. 288 (Wyden) – would extend the Internet Freedom Act moratorium on multiple and discriminatory taxes for 5 years (through December 31, 2006) and provide a permanent ban on taxes on Internet access.[1] S. 288 also includes a Sense-of-the-Senate resolution providing criteria for simplifying the sales and use tax, which if followed by states could enable them to collect use taxes from remote sellers. See the Appendix for further information.

Cost of the ITFA Moratorium and its Possible Expansion: The Federal Internet Tax Freedom Act (ITFA, P.L. 105-277, 10/21/98) imposes a 3-year moratorium (from 10/1/98 through 10/21/2001) on state and local taxes on Internet access, unless such tax was generally imposed and actually enforced before October 1, 1998. S. 288 (107th Congress) proposes both to extend the moratorium, and to remove the grandfather provision so that no state or local government could tax Internet access fees. It has been estimated that such a change would cost Texas about $50 million annually and Tennessee about $17 million annually.[2] State Tax Notes estimates that repeal of the grandfather provision would cost the nine states that are covered (California does not tax Internet access) about $90 million in the first year.[3]

A bill similar to S. 288 was passed by the House – H.R. 3709 (106th Congress) in May 2000. The Congressional Budget Office (CBO) released a "mandates statement" explaining that H.R. 3709 posed a problem under the Unfunded Mandates Reform Act. "Because at least one significant state revenue source – taxes on internet access – would clearly be affected and others might be affected, CBO estimates that the extension and expansion of the moratorium would cause revenue losses that would exceed the annual statutory threshold at some point over the five-year period." Due to the difficulty of estimating the potential revenue loss if with the absence of the ITFA, decided to impose taxes on Internet access. The CBO based its estimate using only the states falling under the ITFA's grandfather provision. The CBO also noted: "In addition, by extending the current moratorium, the bill may affect the ability of state and local governments to collect certain other taxes. Significant and continuous change within the industry, as well as uncertainty about possible legal interpretations of these definitions, make it impossible for CBO to predict the likelihood or magnitude of such effects on state and local budgets."[4]

S. 245 (Smith) - "To make permanent the moratorium on the Federal imposition of taxes on the Internet."

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1 The Internet Tax Freedom Act (Public Law 105-277) passed on October 21, 1998, included a grandfather provision to allow state and local jurisdictions that were imposing and actually enforcing taxes on Internet access prior to October 1, 1998 to continue to do so. The following states fall under this exception: Connecticut (although the tax has been repealed effective 7/1/01), Hawaii (general excise tax), Montana, New Hampshire, New Mexico,, North Dakota, Ohio, South Dakota, Texas (first $25 of monthly access charges are exempt), Tennessee, Washington, and Wisconsin.

2 Brian Krebs, Newsbytes, *Government Technology*, February 16, 2001.

3 Doug Shepard, "State Revenue Officials: Internet Access Tax Repeal Would Cost $90 Million," *State Tax Notes*, 2001 STT 41-30.

4 CBO Mandates Statement on H.R. 3709, May 8, 2000; http://www.cbo.gov.

S. 246 (Smith) - "To extend the moratorium on the [Federal] imposition of taxes on the Internet for an additional 5 years."

COMMENTS ON APPROACHES TO STATE & LOCAL UNIFORMITY AND SIMPLIFICATION

How should uniformity and simplification be achieved? There are various possible approaches. A few of these are outlined below.

Congressional Mandate: For example, in 1959, Congress created uniform nexus rules for the states imposing income taxes on sales of tangible personal property by enacting P.L. 86-272. This law prohibits a state from taxing a foreign corporation's net income derived from activities within the state if those activities consist merely of solicitation of orders for the sale of tangible personal property that are approved, filled, and shipped from outside the state.

Multistate Tax Compact and UDITPA: The Multistate Tax Compact was written in 1966 and became effective in 1967 when seven States had adopted it. A significant stimulus for creating the Compact was the Supreme Court's decision in *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959) and congressional activity following the opinion. In *Northwestern States*, the Court held: "Net income from the exclusively interstate operations of a foreign corporation may be subjected to state taxation, provided the levy is not discriminatory and is properly apportioned to local activities within the taxing State forming sufficient nexus to support the same." Subsequent to the opinion, Congress enacted P.L. 86-272 (see above). This law also called for a study to consider uniform standards for the States in taxing income of interstate businesses.[5] In its consideration of P.L. 86-272 in 1959, the Senate noted that companies engaged in interstate commerce "are in doubt as to the amount of local activities within a State that will be regarded as forming a sufficient 'nexus,' that is, connection, with the State to support the imposition of a tax on net income from interstate operations and 'property apportioned' to the State." The Senate also noted that smaller companies were "fearful" of the costs of compliance primarily due to lack of uniformity in measuring taxable income to be apportioned among the states.[6] Such concerns led to some uniform laws – both through congressional action (P.L. 86-272) and state action (the Compact and UDITPA).

The purposes of the Multistate Tax Compact are to:

"1. Facilitate proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.

2. Promote uniformity or compatibility in significant components of tax systems.

3. Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.

4. Avoid duplicative taxation."[7]

California is a member of the Compact.

The constitutionality of the Compact was upheld by the U.S. Supreme Court in *U.S. Steel Corp. v. Multistate Tax Comm'n.,* 434 U.S. 452 (1978). The Court found that the Compact did not violate the Compact Clause of Article I, 10, clause 3 of the U.S. Constitution ("No State shall, without the Consent of Congress, … enter into any Agreement or Compact with another State …"). Based on precedent, the Court ruled that because the Compact did not increase political power within the States that would encroach upon or interfere with the supremacy of the U.S., it did not violate the Compact Clause. Neither did the Court find that the Compact violated the Commerce Clause or the 14th Amendment. The Court found that the Compact did not enable the States to exercise any powers they could not exercise absent the Compact, and that a State could withdraw from the Compact at any time.

The Compact addresses both income and sales and use tax rules. It includes procedures for interstate audits and creates the Multistate Tax Commission (MTC). Article IV of the Compact contains the Uniform Division of Income for Tax Purposes Act (discussed later).

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5 The report was issued in June 1965 and is referred to as the "Willis Commission Report," because the Commission was chaired by Congressman Willis of Louisiana; House Rpt. No. 565, 89th Congress, 1st Session.

6 Senate Rpt. No. 658, Aug. 11, 1959, 1959 USCCAN 2548 (1959).

7 Article I of the Multistate Tax Compact; available at http://www.mtc.gov/ABOUTMTC/COMPACT.HTM.

The powers of the MTC include:

"(a) Study State and local tax systems and particular types of State and local taxes.

(b) Develop and recommend proposals for an increase in uniformity or compatibility of State and local tax laws with a view toward encouraging the simplification and improvement of State and local tax law and administration.

(c) Compile and publish such information as would, in its judgment, assist the party States in implementation of the compact and taxpayers in complying with State and local tax laws.

(d) Do all things necessary and incidental to the administration of its functions pursuant to this compact."

The MTC currently consists of 45 States; 21 are Compact Members (this includes California), 3 are Sovereignty Members, 18 are Associate Members, and 3 are Project Members.[8] New York is not a member of the MTC.

The Uniform Division of Income for Tax Purposes Act (UDITPA) provides uniform rules for apportioning income for state income tax purposes. "The UDITPA is a tax allocation system approved in 1957 by the National Conference of Commissioners on Uniform State Laws and by the American Bar Association. See 7A U. L. A. 91 (1978)."[9] California adopted UDITPA; the rules can be found at R&T §§ 25120 through 25139.

Other Efforts: Various simplification efforts have been pursued by professional and governmental organizations, such as the American Institute of Certified Public Accountants (AICPA), Committee on State Taxation (COST), Federation of Tax Administrators (FTA), National Governors Association (NGA), and the MTC. For example, the MTC has a list of sales tax simplification ideas.[10] These ideas include uniform registration procedures, uniform sourcing rules for determining where a sale should be taxed, common audit techniques, and limit the frequency of tax law changes. However, because not all states participate in the MTC, such simplification is difficult to achieve.

ADDITIONAL POINTS TO PONDER

• The sales and use tax system has been flawed for decades. It doesn't work well with numerous jurisdictions and interstate sales. Also, it taxes business purchases, which should instead be exempt to avoid pyramiding of the tax. Also, it only applies to tangible personal property, rather than to other types of consumption, such as intangibles and services. Note the date on the following quote:

> Significant problems have been encountered in the application of the [sales and use] tax to interstate transactions. Viewed broadly, these problems appear to stem from a tax system which tends to divide a national market into insulated blocks of consumers, with each sales tax State erecting its own scheme for taxing consumption within its borders. ... [A] firm selling in a number of States is required to meet the peculiarities of the law in each State. If the seller is beyond the jurisdiction of the State or otherwise does not collect the tax, the sale is likely to end up tax free. For local businessmen, this raises the specter of competitive disadvantage; for the States it means a loss of revenue. All things considered, the situation appears one in which it would appear entirely possible to fashion practical solutions to practical problems.
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> *State Taxation of Interstate Commerce ("Willis" Report) June 1965*

• The key sales and use tax problem for state and local government is the inability to effectively collect the use tax on remote sales. While a solution will likely take many years, in the mean time, nothing is being done in most states, including California, to educate consumers about the use tax. A few states have a line on the state individual income tax form for the use tax (such as Michigan, North Carolina, Maine, Kentucky).

• The biggest problem for vendors is the complexity of the system caused by over 7,000 taxing jurisdictions and multiple sets of rules. Simplicity would require some level of uniformity, which is very difficult to achieve due to state sovereignty. The states do not have a strong history of adopting uniform rules on their own.

• Uniformity of rules among taxing jurisdictions is difficult to attain and to sustain. Local jurisdictions will prefer to have some control over their tax rate and base as opposed to having it set/fixed by a group of states or the federal government.

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[8] See http://www.mtc.gov/ABOUTMTC/Aboutmtc.htm.

[9] *Asarco Inc. v. Idaho State Tax Comm'n.,* 458 U.S. 307 (1982), fn. 3.

[10] See http://www.mtc.gov/STSpage.htm.

- Reaching uniform definitions is difficult. For example, the SSTP proposes that one fact that distinguishes candy from food is that candy doesn't contain flour. Thus, it would be necessary to read the ingredients listed on a package to determine if it is "candy" (which some states tax) or food (which some states may treat as exempt from tax). Since the uniform definitions are needed only to allow a state to be able to treat something as exempt from tax, perhaps it is the use of exemptions that is the complexity cause, not the definitions. If all tangible personal property were subject to sales tax, there would be no need for definitions of food, clothing and other items. To provide relief to low-income individuals for payment of sales tax on food, another type of relief could be provided, such as through the income tax. Of course, defining "tangible personal property" can also raise problems, but not as many. And, that problem could be avoided by subjecting all consumption (tangible and intangible personal property and services) to sales/use tax and lowering the tax rate.

- The sales/use tax is just one form of consumption tax. Perhaps other approaches should be examined, such as a valued added tax. Or, consumers could compute sales/use tax based on the formula: Income – savings = consumption. Of course, this system would not be simple due to the need for detailed recordkeeping to track changes in annual savings.

- Sales tax is just one issue: While the bulk of discussions on application of tax to e-commerce transactions today have pertained to sales tax and international taxes, there are issues in all types of taxes, including federal and state income taxes, telecommunication taxes, and perhaps even property taxes. As surviving dot-coms begin to generate income,[11] some of the state income tax issues will become more pressing. Effective reform of tax systems, should really consider all types of revenue that each jurisdiction imposes.

[11] A March 2001 study by ActivMedia Research has reported that 50% of online B2C vendors are generating a profit. See Clare Saliba, "Study: Half of E-tailers Are Turning a Profit," *E-Commerce Times*, March 13, 2001; http://www.ecommercetimes.com/perl/printer/8142/.

Appendix—Simplification Perspective of SSTP versus Federal Proposals of the 107th Congress

As discussed earlier, both S. 288 and S. 512 of the 107th Congress include a list of factors deemed to be necessary elements of a state law providing for a simplified sales and use tax system for remote sales. These bills also state that adoption of such a simplified system would lead to a joint resolution allowing the state to collect sales and use tax on remote sales. The criteria laid out in S. 288 and S. 512 are not entirely the same and are not entirely the same as in the Streamlined Sales Tax Project. The following chart compares these proposals. The chart also notes where the National Conference of State Legislatures (NCSL) amended the SSTP.

Note: The following information is a summary, for specific details of the proposals, the full text of the SSTP Model Act and Agreement, as well as S. 288 and S. 512 should be reviewed.

Feature	SSTP	Federal Proposals: S. 288 and S. 512
Seller registration.	Requires an online sales and use tax registration system be used by the member states.	Requires a centralized, one-stop, multistate registration system.
Uniform definitions of goods and services.	Definitions provided for clothing, clothing accessories or equipment, sport or recreational equipment, protective equipment, food and food ingredients (which excludes alcoholic beverages and tobacco), candy, dietary supplements, soft drinks, food sold through vending machines, and prepared food. The importance of the definitions is in defining what is taxable or exempt under the system. For example, because "candy" is separately defined, it would be possible for a state to tax "candy" but to exempt "food." **NCSL:** Allows states to levy a lower rate on food, clothing, electricity, gas, and other specified items. Also, all uniform definitions were deleted and will undergo further review.	Requires uniform definitions for goods and services.
Other uniform definitions.	Definitions provided for delivery charges, purchase price, retail sale, sales price.	No specific requirements.
Level of administration.	State level administration must be provided for local sales and use taxes.	Same.
State and local tax base.	Through 12/31/05, all local jurisdictions in the state must have a common tax base. After that date, the local tax base must match that of the particular state.	No specific requirements.

Feature	SSTP	Federal Proposals: S. 288 and S. 512
Tax rates.	May not have multiple tax rates on items of personal property or services after 12/31/05. Local jurisdictions levying both a sales and use tax must use the same rate for each. Member states must "provide and maintain a database that assigns each five (5) digit and nine (9) digit zip code within the State to the proper tax rates and jurisdictions."	S. 288: Requires a single uniform statewide rate on all transactions – one-rate-per-state. S. 512: Requires a single, uniform Statewide use tax rate on all remote sales for sellers who adopt the "Compact." Allows for use of a weighted average tax rate. However, if a State "dramatically" simplifies its sales and use tax system "so that remote sellers can use information provided by the State to identify the single applicable rate for each sale, may require a remote seller to collect the actual applicable State and local sales or use tax due on each sale made in the State if the State provides such seller relief from liability to the State for relying on such information provided by the State."
Rate changes.	Member states must make a "reasonable effort" to give sellers as much advance notice as practicable regarding rate changes, limit the effective date to the first day of a quarter, notify sellers of legislative changes in the tax base.	No specific requirements.
Math.	Tax amount is carried to third decimal place. Round down if under ½ of one cent, otherwise round up. **NCSL:** Rounding provision deleted and to undergo further review.	No specific requirements.
Sales tax holidays.	The state may not apply an exemption after 12/31/03 unless the exempted item has been defined under the uniform definition provisions. **NCSL:** Provision deleted and to undergo further review.	No specific requirements.
Software certification.	CAS is certified.	Requires uniform procedures for certification of software relied upon by vendors to determine tax rates and taxability.
Sourcing rules.	Sourcing rules are the same for tangible goods, digitized items, and services (other than telecommunications). The rules: "a. When the product is received by the purchaser at a business location of the seller, the sale is sourced to that business location. b. When the product is not received by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser occurs, including the location indicated by instructions for delivery to the purchaser, known to the seller. c. When (a) and (b) do not apply, the sale is sourced to the location indicated by a address for the purchaser that is available from the business records of the seller that are maintained in the ordinary course of the seller's business when use of this	Requires uniform rules for attributing transactions to particular taxing jurisdictions. S. 288 also provides that such rules be simple. S. 288: For goods or services delivered via the Internet, an "origin State default system" is required for transactions where the customer's location is not disclosed during the transaction. Under this rule, the seller would determine the sales or use tax using the law of the State where the seller is located. In addition, the seller would be permitted to rely upon information provided by the customer.

	address does not constitute bad faith. d. When (a), (b), and (c) do not apply, the sale is sourced to the location indicated by an address for the purchaser obtained during the consummation of the sale, including the address of a purchaser's payment instrument, if no other address is available, when use of this address does not constitute bad faith. e. When none of the previous rules of (a), (b), (c), or (d) apply, including the circumstance where the seller is without sufficient information to apply the previous rules, then the location will be determined by the address from which tangible personal property was shipped, from which the digital good was first available for transmission by the seller, or from which the service was provided (disregarding for these purposes any location that merely provided the digital transfer of the product sold.)" A purchaser who plans to use the items at multiple locations must remit the required tax to the proper jurisdictions. *Query*: Are the sourcing rules intended to apply for all sales, or only for remote sales?	
Exempt purchasers and transactions.	General guidelines are provided for transactions where the purchaser is claiming a tax exemption. Sellers must maintain proper records of such transactions and provide them to a member state when requested. Member states must relive sellers from tax if they have followed the exemption procedures of the Agreement.	S. 288: Requires uniform rules that designate and identify purchasers and transactions that are exempt from sales and use tax, "including a database of all exempt entities and a rule ensuring that reliance on that database immunizes sellers from liability." S. 512: Requires uniform procedures for the treatment of exempt purchases and relief from liability for sellers relying on such procedures.
Exempt small sellers.	No rule.	Use tax collection exemption for remote vendors with gross annual sales less than a specified threshold of not less than $5 million.
Tax returns.	Requires only one return per taxing period per seller per state. Returns must be due no sooner than the 20th day of the month following the month in which the transaction occurred. All states to be capable of accepting electronically filed returns by 2003.	Requires uniform tax returns and remittance forms. S. 288: Requires a "single filing for all sales."
Remittances	Requires only one remittance per tax return unless seller collects over $30,000 in sales and use tax during the prior calendar year. Electronic remittances possible.	Requires uniform tax returns and remittance forms.
Electronic filing.	"Require, at each member state's discretion, All Model 1, 2, and 3 sellers to file returns electronically. It is the intent of the member states that all member states have the capability of receiving electronically filed returns by January 1, 2003.	S. 288: Requires uniform electronic filing and remittance methods. S. 512: Requires consistent electronic filing and remittance methods.

Feature	SSTP	Federal Proposals: S. 288 and S. 512
Audit procedures.	"Member states must conduct, or authorize others to conduct on their behalf, all audits of the sellers registered under this Agreement, and local jurisdictions shall not conduct independent sales or use tax audits of sellers registered under this Agreement."	Requires uniform audit procedures and an option that a seller agreeing to be subject to audit by any State won't be subject to more than one audit.
Bad debts.	Sellers must be allowed a deduction for bad debts. **NCSL:** Provision deleted and to undergo further review.	S. 288: Requires uniform bad debt rules. S. 512: No provision.
Privacy.	A Model 1 CSP must perform without retaining the personally identifiable information of customers; testing is required to verify.	Must provide protection for consumer privacy.
Vendor compensation.	Model 1 CSPs to be compensated by the states. Model 2 and 3 sellers will obtain compensation for 24 months and other compensation allowed by state law. **NCSL:** Above provision to remain pending completion of a joint public/private study of compliance costs.	Reasonable compensation for tax collection by vendors must be provided.
Amnesty	States participating in the SSTP are to give amnesty for uncollected or unpaid sales and/or use tax to vendors who register. Exceptions to amnesty exist if the vendor was registered with the state within the 12-month period preceding the State's participation in the SSTP Agreement, the vendor received notice of an audit which is not yet resolved, or there is fraud or intentional misrepresentation.	No provision.
Continued role of SSTP and State Advisory Committee.	Agreement can be amended by the SSTP prior to becoming effective (when at least 5 states have signed on). After that point, the Committee will be formed to continue the work of the SSTP. **NCSL:** States passing the Model Act may send up to four representatives to participate in multistate discussions to finalize the terms of the agreement. After 7/1/03, only states passing the Model Act and Agreement have voting authority. The SSTP becomes an advisory group to the governing states and not changes adopted by the SSTP as of 1/27/01 are binding on the governing states or the agreement.	N/A

Feature	SSTP	Federal Proposals: S. 288 and S. 512
Role of Congress	None specified. “This Agreement is among individual cooperating sovereigns in furtherance of their governmental functions. The Agreement provides a mechanism among the member states to establish and maintain a cooperative, simplified system for the application and administration of sales and use taxes under the duly adopted law of each member state.”	S. 288: No state may require a remote seller to collect or remit sales or use tax until Congress provides such authority to the State. Such authority would be derived from adoption of a joint resolution of Congress. Such authority will not be available if the State’s law imposes multiple or discriminatory taxation. S. 512: Authorizes the states to enter into an Interstate Sales and Use Tax Compact that describes a simplified system (as noted in S. 512). This authorization expires if the Compact has not been formed before January 1, 2006. To be formed, the Compact must have 20 States join. The Compact allows states to collect use tax from all sellers not qualifying for the de minimis exception.
Nexus for other purposes.	Section 6.e. of the Model Act provides: “No Nexus Attribution: The Agreement must provide that registration with the central registration system and the collection of sales and use taxes in the signatory states will not be used as a factor in determining whether the seller has nexus with a state for any tax.”	S. 288: Must provide “clear standards for determining the nexus of business activity, for tax purposes, that limit business activity tax nexus to sellers that have continuous and systematic contacts with the State.” S. 512: “In general, nothing in this Act shall be construed as subjecting sellers to franchise taxes, income taxes, or licensing requirements of a State or political subdivision thereof, nor shall anything in this Act be construed as affecting the application of such taxes or requirements or enlarging or reducing the authority of any State or political subdivision to impose such taxes or requirements.” Both S. 288 and S. 512 provide that a State’s authority to collect use tax from a seller has no effect on nexus determinations for other tax purposes.

For a list of states that have introduced legislation to consider or adopt the SSTP Model Act and Agreement, see information on the Streamlined Sales Tax Project at:

http://www.cob.sjsu.edu/facstaff/nellen_a/e-links.html.